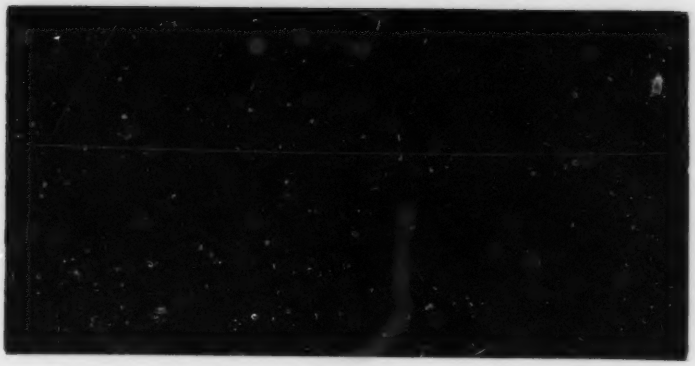

THE SOCIAL PLANNING and RESEARCH COUNCIL of Hamilton and District

155 JAMES STREET SOUTH, 6TH FLOOR HAMILTON, ONTARIO L8P 3A4 TELEPHONE 522-1148

TAXATION IN CANADA:

THE REPORT OF THE

TAXATION REVIEW TASK FORCE

June 1992

SOCIAL PLANNING AND RESEARCH COUNCIL OF HAMILTON AND DISTRICT

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PREAMBLE

There are very few areas of public policy which generate as much controversy as the issue of taxation. The purpose of this paper was to examine the Canadian approach to taxation from one particular perspective - a comparative analysis of Canada's system of taxation and expenditure, relative to the approaches utilized in other western industrial nations.

There is an immense variety of approaches to taxation within the industrial world. Individual countries vary dramatically in terms of the level of taxation, types of taxation and patterns of government expenditure. The diversity of these patterns challenge the notion that there is one "correct" approach to taxation within national economies. At the same time, it must be recognized that the differences in taxation between nations are, to a certain extent, reflective of differences in cultures, mores and norms among national societies.

It should not be assumed, therefore, that taxation systems can simply be transplanted from country to country. An approach to taxation which "works" in West Germany may be inappropriate for Canada, given differences in traditions, cultures and institutions.

At the same time, however, the experience of other nations can be instructive with respect to the ongoing debate about taxation in Canada. It is with this purpose in mind, that this report has been released by the SPRC as a contribution to the ongoing discussion of taxation issues.

I. INTRODUCTION

This report presents the summary of a two-year review of the Canadian tax system, for the purpose of developing a comprehensive set of taxation policies for the Social Planning and Research Council of Hamilton and District. This review has generated a total of twelve background papers which have relied extensively on comparative data from other western industrial nations.

The issue of taxation and its social/economic consequences is an area of inquiry which is severely clouded by ideological and philosophical considerations. In carrying out this review, therefore, the SPRC attempted to rely upon empirical data and studies in order to sort out the ideological theory from empirically supportable conclusions.

The SPRC Taxation Review Task Force was deliberately composed to represent a variety of ideological/philosophical orientations and the conclusions which have been drawn from the review, reflect the consensus among its members.

Through a process of relying upon empirical data, presented to an ideologically heterogeneous group of task force members, the SPRC has attempted to contribute to the ongoing debate about tax reform in a relatively non-ideological manner.

The results of this analysis has called into question many of the ideological generalizations which tend to mark debates about tax policy. These results have consequently reinforced our belief about the urgent need to review our system of taxation in a way that stresses objective appraisal and the development of a consensus among the various sectors that comprise our society about the effectiveness and the fairness of our current systems of taxation.

This project relied extensively upon studies and data from the Paris-based organization of Economic Co-operation and Development. The twenty-two member nations of the OECD represent the most developed western industrial nations in the world and, therefore, represent a valid point of comparison for Canadian statistics. The OECD has developed standardized approaches to national accounts and other statistical indicators which allow for meaningful comparisons between nations.

The results of this inquiry are presented in this summary report, as they relate to critical taxation issues - the level of taxation in Canada, the progressivity of Canadian taxation, corporate taxation, tax expenditures, and the deficit. The report also contains two chapters dealing with Japanese and American approaches to taxation and public expenditures.

All of the material contained in this summary report is drawn from more detailed analyses contained in twelve discussion papers which are also available from the SPRC. These discussion papers are described in an Appendix to this report.

II. THE TAX BURDEN

There are very few areas of public policy that result in more debate than the issue of taxation burden. No one enjoys paying taxes and, as a consequence, the level of taxation in nations is a subject of continual discussion. Most tax-payers would prefer to use their income for the purpose of personal consumption or savings and, from that perspective, people are wary about high levels of taxation.

These concerns about levels of taxation are compounded by controversy pertaining to the effects of taxation on the economic health of the nation. There is a general belief that taxation is harmful, to the extent that it "removes" spending from the private sector and restricts the Gross Domestic Product (GDP). At the same time, however, it is recognized that taxation does not "remove" money from the economy - it simply redistributes it. Taxation revenues simply "pass through the hands" of government before entering the private sector through government contracts or through the personal purchases of civil servants or other recipients of government funding. Governments use taxation revenues to build roads, bridges, schools, and hospitals; to rent office space, buy office supplies and equipment; to pay civil servants who then spend their money in the private economy; to subsidize senior citizens or the unemployed, who then spend their money in the private sector.

The methods chosen by government to raise money through taxation, however, can affect economic activities. Some methods, for example, are more efficient than others. Some methods may have more of an effect upon Canada's competitiveness than others.

The major effect of government finance on the economy is related to what the government does with the money. It is more a question of expenditures than taxation revenues. If expenditures provide effective "value-for-money" to the Canadian public and result in the creation of long-term wealth for future generations, then it is difficult to conclude that they represent destructive forces in the economy.

This conclusion is supported by a variety of data and studies pertaining to the different tax burdens in national economies. The most frequent measure of "tax-burden" is the percentage of a country's GDP which is devoted to revenues to all levels of government.

As presented in Table II.1, the size of tax-burdens among western industrial nations vary dramatically. In 1986, tax-burdens varied from a high of 53.5% in Sweden to a low of 22.7% in Turkey. It is also notable that the magnitude of the tax-burden in Canada is relatively low, by international standards.

Based upon empirical evidence from the actual economic performance of western industrial countries during the 1970s and 1980s, there does not appear to be any predictable relationship between the level of tax-burdens and the rates of economic growth, defined as growth in the GDP. A previous analysis by

the SPRC indicated that there was no statistical relationship between the level of tax-burden in 22 western industrial countries and their subsequent rates of economic growth.[1]

The results of these analyses suggest that the overall tax-burden in Canada could increase, without necessarily jeopardizing economic growth. At the same time, we recognize that the type of taxation utilized, the manner by which it is introduced and the type of expenditures which could result from increased taxation, could have negative economic consequences.

We do believe, however, that current theories about the effects of taxation on the economy, need to be reviewed in the light of empirical evidence. We note, for example, that a few recent studies have called into question the validity of some "truisms" about the relationship between specific forms of taxation and economic growth.

For example, a recent study by King and Fullerton (1983) for the National Bureau of Economic Research examined differences in taxation on capital between the U.S., U.K., Sweden and West Germany to test the prevalent assumption that higher rates of taxation on income from capital impacts negatively upon economic development through the diversion of funds from private investment to government purposes. Their report stated:

> "The results are surprising to say the least. If we rank the countries by their average annual growth of GDP, we obtain exactly the same order as when we rank by effective tax rates. Germany has the highest overall effective tax on income from capital and the highest growth rate. The U.S. is second in both categories and Sweden is third. The U.K. has the lowest overall effective tax on income from capital and the lowest growth rate".

A Canadian study by Daly, Mercier and Schweitzer (1989) for the Economic Council of Canada tested, among other things, the Canadian truism that favourable taxation rates for manufacturing industries are necessary to ensure international competitiveness. Their conclusions were as follows:

> "As far as industries are concerned, Canada and, to a lesser extent, the United Kingdom, treated investment in manufacturing more favourably than those in commerce and in other industry, whereas the United States and Japan did not. Both of the foregoing findings with respect to Japan are interesting because they cast doubt on the widespread presumption held in Canada that preferential tax treatment of investment in manufacturing and in machinery is necessary to ensure this country's international competitiveness. Japan's economic performance has been outstanding in the absence of such tax preferences".

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[1]Social Planning and Research Council of Hamilton and District. Taxation Burdens and Economic Growth: International Comparisons Discussion Paper #8. Taxation Review Task Force, June 1990.

Another recent review of taxation systems in the U.S., Britain, Japan and West Germany, Kuttner (1987), reached the following conclusion:

> "Far the most important conclusion is that taxation doesn't matter all that much" (p.227).

He summed up the general conclusions in the following way:

> "Their tax systems serve to indicate that whatever the secret of Japanese and German success, it isn't low taxes, flat taxes or tax preferences aimed at capital investment. Far better candidates would be financial systems that engender high savings rates and low capital costs and social systems that produce a high degree of cohesion and co-operation" (pg.228).

All of the studies quoted above have produced conclusions which are inconsistent with prevailing theories concerning the relationship between taxation and the economy. They suggest that these theories should be further tested through a rigorous empirical analysis based upon the actual performance of national economies.

TABLE II.1

TOTAL TAXATION REVENUES AS A PERCENTAGE OF GROSS DOMESTIC PRODUCT AT MARKET PRICES 1986

Sweden	53.5%
Denmark	50.6%
Norway	49.8%
Netherlands	45.5%
Belgium	45.4%
France	44.2%
Austria	42.6%
Luxembourg	42.4%
Ireland	40.2%
U. K.	39.0%
Finland	38.4%
Germany	37.5%
Greece	36.7%
Italy	36.2%
Canada	33.2%
New Zealand	32.9%
Switzerland	32.6%
Portugal	32.4%
Australia	31.4%
Spain	30.4%
U.S.	28.9%
Japan	28.8%
Turkey	22.7%
O.E.C.D.	38.1%
E.E.C.	40.0%

Source: Revenue Statistics of OECD Member Countries. Paris: OECD, 1988.

III. TRENDS IN TAXATION (1965 TO 1986)

Figure III.1 presents the trend in tax burdens for Canada, the U.S. and the European Economic Community (EEC) for selected years between 1965 and 1986. There was very little difference between these three jurisdictions in 1965. The EEC member nations averaged 27.1% of GDP, the U.S. 25.9% and Canada was lowest with 24.5%.

From 1965 to 1970, there was a rapid growth in tax loads in all three areas - particularly in Canada which went from the lowest to the highest among the three units.

From 1970, the trends in the three jurisdictions diverged substantially. During the seventies, the rate of increase in Canada and the U.S. moderated, while tax loads in the EEC continued to escalate. During the 1980's, both Canada and the U.S. showed a decrease, while the EEC tax load continued to increase. By 1980, the tax loads were widely divergent with Canada occupying a mid-point position.

By 1986, Canada ranked 15th out of the 23 OECD member nations. It is noteworthy that these differences in tax loads have significant revenue consequences. If, for example, Canada had devoted the proportion of its GDP to taxation as the U.K., an additional 29 billion dollars in revenues would have been generated. If these revenues had gone to the Federal Government, the Federal deficit would have been eliminated. In the extreme case, the application of the Swedish tax load to our GDP would have generated an additional 100 billion dollars - leaving the Federal Government with a surplus of between 60 and 70 billion. At the other end of the continuum, the application of the U.S. tax load would have increased the Federal deficit by 22 billion.

In generating taxation revenues, governments have a wide variety of tax vehicles available to them. The accounting system that is utilized by the Organization for Economic Co-operation and Development (OECD) utilizes six general categories of taxation -

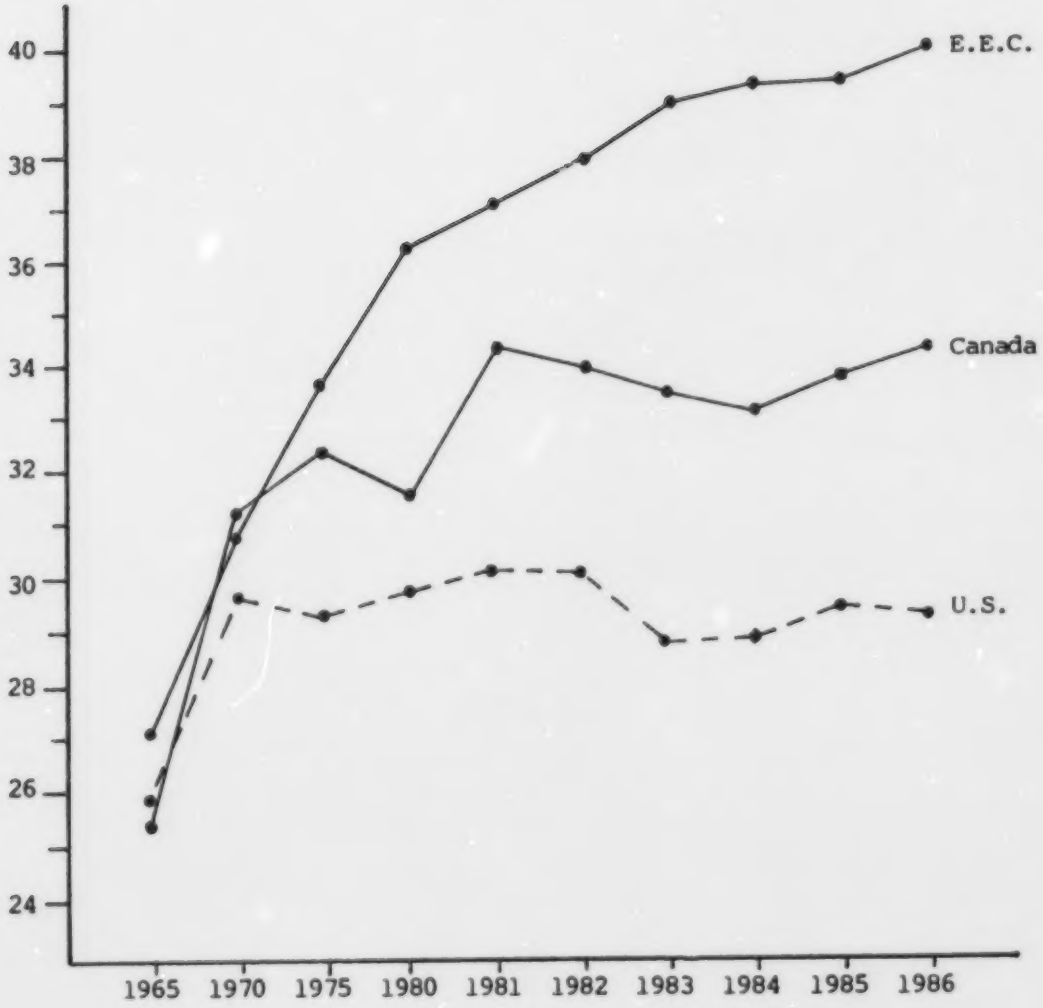
1. Taxes on Personal Income
2. Taxes on Corporate Income
3. Social Security Contributions
4. Taxes on Payroll and Workforce
5. Taxes on Property
6. Taxes on Goods and Services

Each of these general headings include a variety of more specific categories and sub-categories.

The taxes on personal income and corporate income are self-explanatory and reflect the Canadian nomenclature of personal income tax and corporate income tax, respectively.

FIGURE 111.1

TAX REVENUES AS A PERCENTAGE OF GDP CANADA, U.S. AND E.E.C.



Social security contributions cover a wide variety of payments which are made to government, specifically for social security purpose. In Canada, direct payments for C.P.P., Unemployment Insurance and hospital insurance fall into this category.

Taxes on Payroll and Workforce refer to special taxes levied on employers and employees which are not earmarked for social security purposes. Canada does not report any taxation of this nature.

Taxes on Property includes any taxation which is levied on the use, ownership or transfer of property. This includes "property taxes" as they are known in Canada as well as estate taxes, inheritance taxes and taxes on financial transactions.

Taxes on Goods and Services include a multiplicity of categories, the largest of which are sales taxes, value-added taxes, excise taxes, import/export taxes and taxes on the extraction, processing or production of natural resources.

Each of these general categories are analyzed separately in this chapter of the report. The figures which are utilized, indicate the percentage of total taxation revenues which are derived from each source for the OECD member nations. The figures, therefore, represent the extent to which each country is dependent on each type of taxation for their public revenues.

Corporate Income Tax

Canada's decreased dependence upon corporate income tax during the past twenty years has "brought it into line" with most other Western industrial nations, although wide variation does occur among these nations. During the twenty-year period between 1965 and 1986, the dependence of European nations upon corporate sources remained relatively unchanged, while North American dependency on this source dropped significantly. By 1986, Japan showed the highest dependence on this source, followed by Luxembourg, Norway, Turkey and the U.K. Canada ranked 7th among the 21 nations for which data was available (see Figure III.2 and Table III.3).

Personal Income Tax

In comparison with European nations, Canada had a somewhat higher degree of dependence on personal income taxes. Canada and the U.S. have shown increased dependence on this source since 1965. As a result of American tax cuts in 1986, Canada surpassed the U.S. in that year for the first time. The European nations, on the other hand, showed increased dependence until 1980 and then a decreased dependence during the eighties.

By 1986, Canada ranked 6 out of 21 reporting nations with respect to our dependence upon personal income tax (see Figure III.4 and Table III.5).

FIGURE III.2

TAXES ON CORPORATE INCOME AS A PERCENTAGE OF TOTAL TAXATION

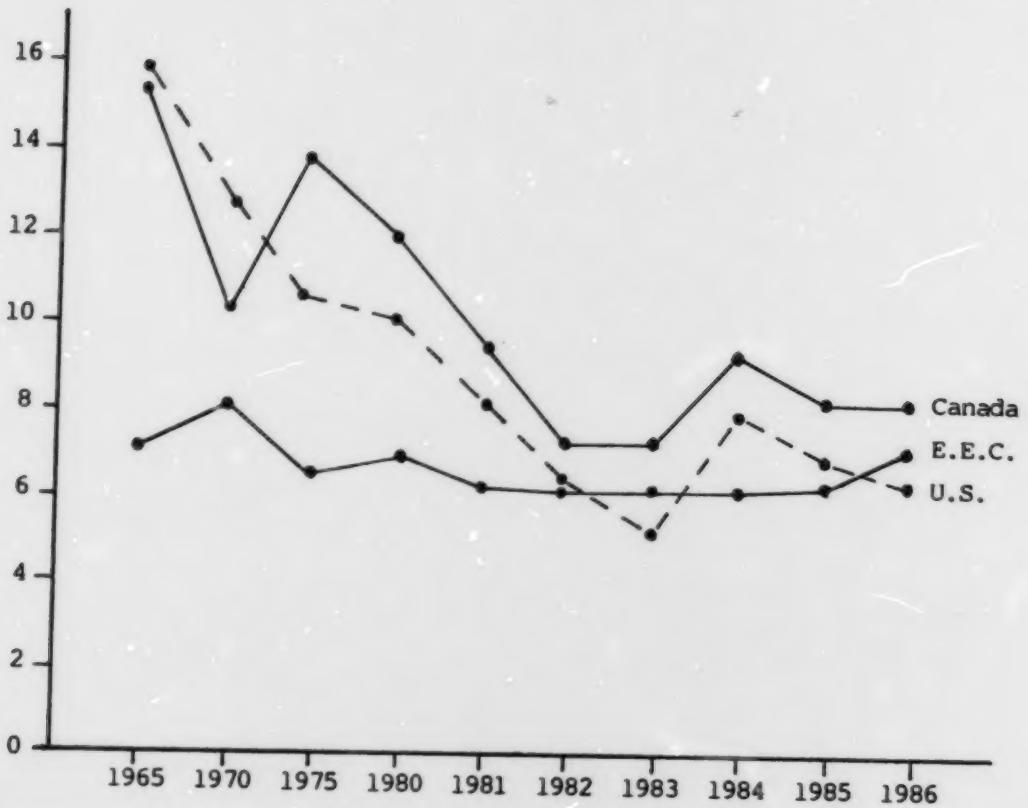


TABLE III.3

TAXES ON CORPORATE INCOME AS A % OF TOTAL TAXATION IN 1986

Japan	20.7%
Luxembourg	16.7%
Norway	13.3%
Turkey	12.1%
U.K.	10.3%
Australia	9.0%
Canada	8.1%
Netherlands	7.3%
New Zealand	7.0%
U.S.	7.0%
Belgium	6.6%
Switzerland	6.2%
Denmark	6.2%
Germany	6.0%
Spain	5.9%
France	5.1%
Sweden	4.7%
Greece	4.0%
Finland	3.7%
Ireland	3.5%
Austria	3.4%
O.E.C.D.	7.9%
E.E.C.	7.2%

FIGURE III.4

TAXES ON PERSONAL INCOME AS A PERCENTAGE OF TOTAL TAXATION

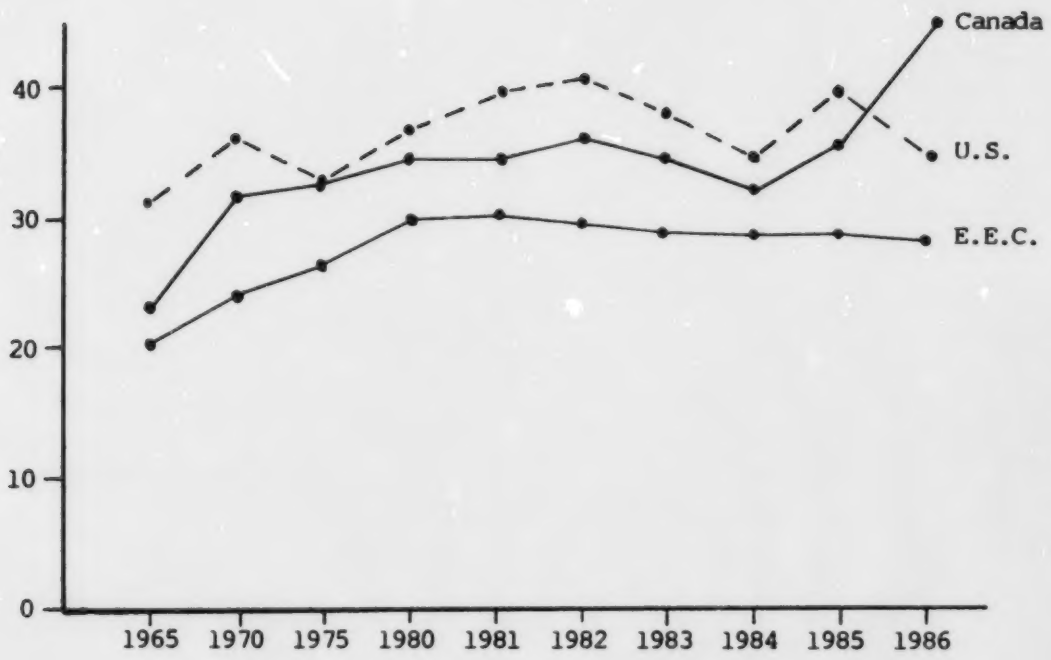


TABLE III.5

TAXES ON PERSONAL INCOME AS A % OF TOTAL INCOME IN 1986

New Zealand	62.6%
Finland	48.1%
Denmark	47.8%
Australia	46.6%
Sweden	38.0%
Canada	37.0%
U.S.	35.4%
Switzerland	34.9%
Belgium	33.7%
Ireland	32.6%
Germany	28.6%
U.K.	27.9%
Turkey	26.9%
Luxembourg	26.5%
Japan	25.1%
Austria	23.4%
Norway	22.8%
Netherlands	20.3%
Spain	17.7%
Greece	13.1%
France	13.0%
O.E.C.D.	31.5%
E.E.C.	26.1%

Social Security Contribution

Canada has traditionally made significantly less use of direct contributions to social security than most other countries. In 1986, we ranked 18th in our dependency on this source of revenue - only Turkey, Finland and Denmark ranked lower than Canada.

A previous analysis by the SPRC reported that most European nations received a much greater share of their tax revenues from employer contributions to social security than from corporate income tax. It appeared, therefore, that the lower rate of dependence upon corporate income taxes by European nations is more than offset by an extensive use of employer contributions to social security.

When these two sources of taxation are combined (Table III.8), Canada ranked 17th our of 22 nations with respect to our dependence upon these sources (see Figure III.6, Tables III.7 and III.8).

Taxes on Property

During the past twenty years, there has been a general decrease in dependence upon property taxes in the U.S., Canada and the EEC, although North America has tended to be more dependent on this revenue source. In 1986, Canada ranked 4th out of 23 nations in our dependence upon this revenue source (see Figure III.9 and Table III.10).

Although Canada was similar to the U.S., U.K. and Japan in our high level of reliance upon property tax revenues, a previous analysis by the SPRC highlighted some notable differences in the type of property taxation which was utilized -

a) Japan makes less use of taxation on immovable properties (e.g. taxes of residential/commercial/industrial property) and a greater use of estate taxes and the taxation of financial and capital transactions.

FIGURE III.6

SOCIAL SECURITY CONTRIBUTIONS AS A PERCENTAGE OF GDP

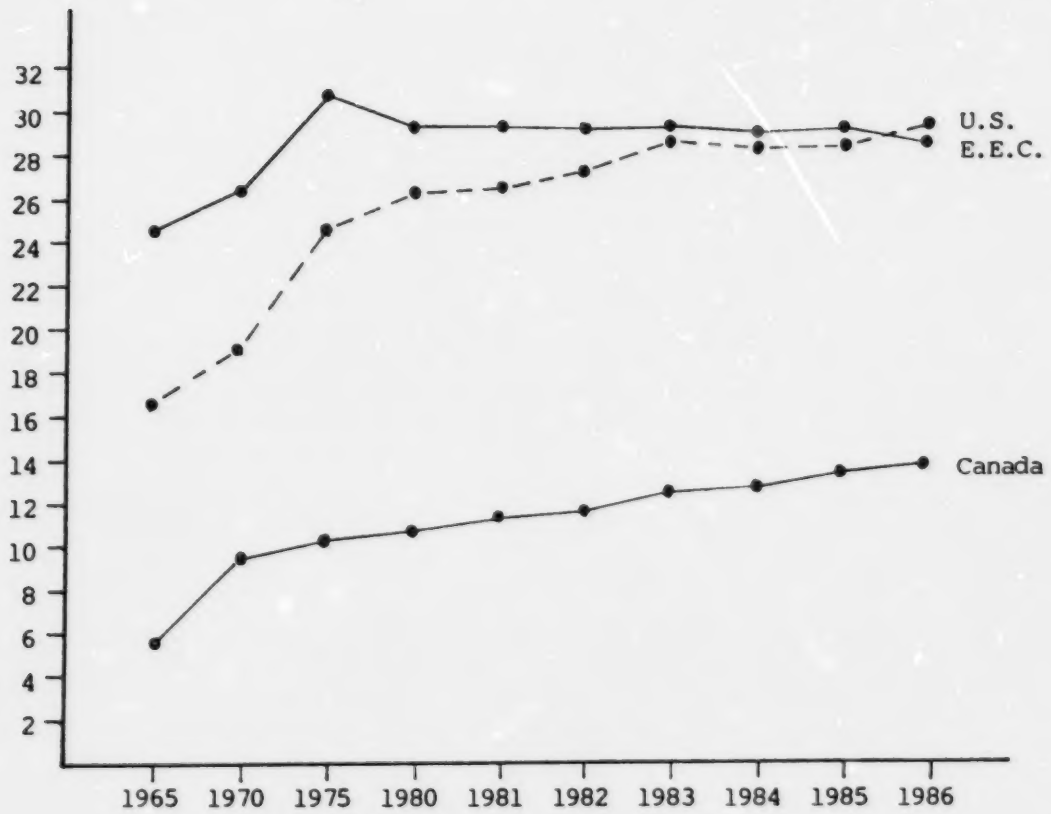


TABLE III.7

SOCIAL SECURITY CONTRIBUTIONS AS A % OF TOTAL REVENUES

France	42.7%
Netherlands	42.5%
Spain	39.1%
Germany	37.2%
Italy	34.3%
Belgium	33.6%
Greece	32.6%
Austria	31.9%
Switzerland	31.6%
U.S.	29.8%
Japan	29.8%
Portugal	28.1%
Luxembourg	25.6%
Sweden	25.0%
Norway	22.2%
U.K.	17.9%
Ireland	14.8%
Canada	13.7%
Turkey	12.8%
Finland	9.0%
Denmark	3.1%
O.E.C.D.	24.2%
E.E.C.	29.2%

TABLE III.8

CORPORATE INCOME TAX AND EMPLOYER SOCIAL SECURITY CONTRIBUTIONS AS A % OF TOTAL REVENUES

Japan	36.0%
Spain	35.3%
France	32.5%
Luxembourg	30.4%
Italy	29.4%
Sweden	28.8%
Norway	28.2%
Germany	25.0%
Netherlands	24.6%
U.S.	24.2%
Belgium	23.8%
Turkey	19.6%
U.K.	19.4%
Austria	19.2%
Greece	18.2%
Switzerland	17.2%
Canada	16.8%
Finland	12.8%
Ireland	12.6%
Australia	9.0%
Denmark	7.4%
New Zealand	7.0%

FIGURE III.9

TAXES ON PROPERTY AS A PERCENTAGE OF TOTAL TAXATION

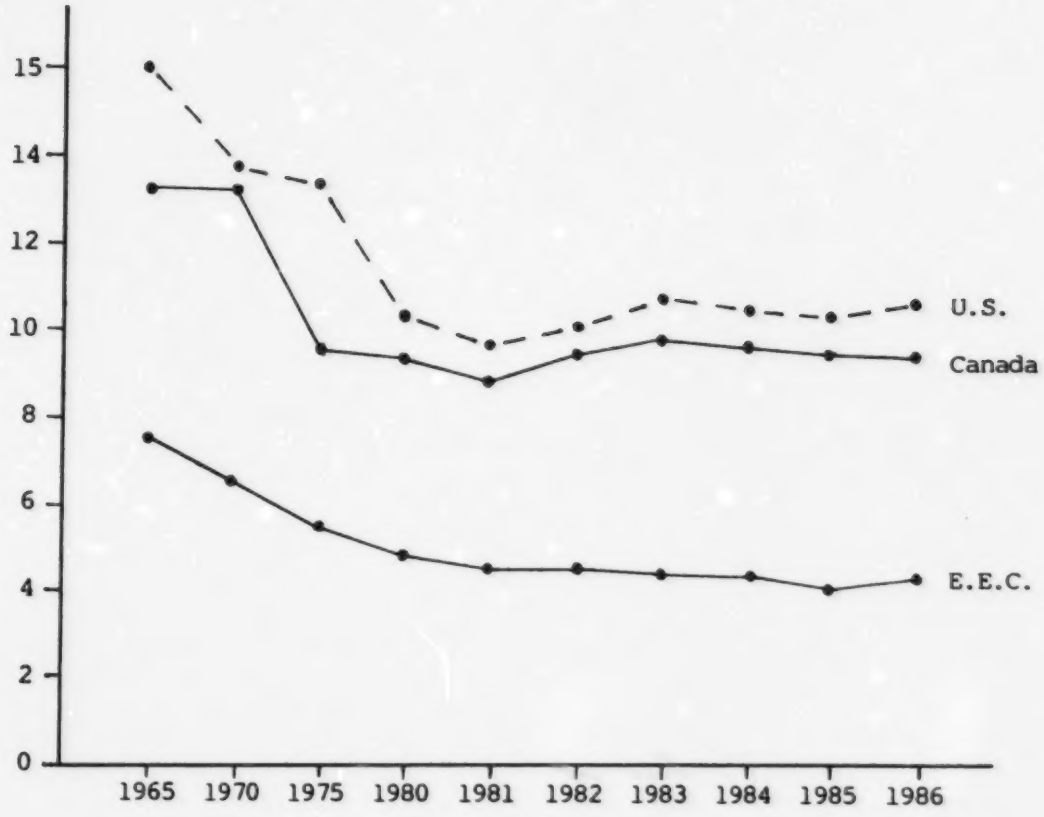


TABLE III.10

TAXES ON PROPERTY AS A % OF TOTAL TAXATION REVENUES IN 1986

U.K.	12.9%
Japan	10.9%
U.S.	10.3%
Canada	9.4%
Switzerland	8.4%
Australia	8.0%
Luxembourg	6.2%
France	4.8%
Denmark	4.7%
Ireland	3.9%
Netherlands	3.6%
Turkey	3.3%
Spain	3.2%
Finland	3.1%
Germany	3.1%
Greece	2.7%
Italy	2.7%
Austria	2.4%
Norway	2.1%
Portugal	1.9%
Belgium	1.9%
New Zealand	1.7%
O.E.C.D.	4.9%
E.E.C.	4.3%

b) Canada is unique among these countries with respect to its very minimal use of estate taxes and its non-use of taxation on financial and capital transactions.

Taxes on Goods and Services

Canada has traditionally been close to the European community with respect to our dependency on consumption taxes. For most of the period between 1965 and 1986, we had a slightly higher dependence than the European community, but this position reversed in 1986. The U.S. has made a significantly less use of this source.

It is important to note that this data pre-dates the introduction of the Goods and Services Tax in Canada.

In 1986, Canada ranked 12th out of the 23 reporting nations with respect to this revenue source (see Figure III.11 and Table III.12).

Financing the Welfare State

Table III.13 presents the distribution of tax revenues across the major categories for the 5 countries with the greatest 1986 tax load (welfare states) and the 5 countries with the lowest tax load (free-market states). There were very few consistencies within each group.

Sweden and Denmark received the largest share of their revenues from personal income tax, as did the U.S. and Australia on the free-market side.

The Netherlands received their largest share from social security payments, as did Japan and Spain. Both Norway and Turkey received their largest share from goods and service taxes.

In summary, then, the only similarity among welfare states relates to their higher than average tax loads. The vehicles used for generating those revenues varied significantly among the countries.

FIGURE III.11

TAXES ON GOODS AND SERVICES AS A PERCENTAGE OF TAXATION

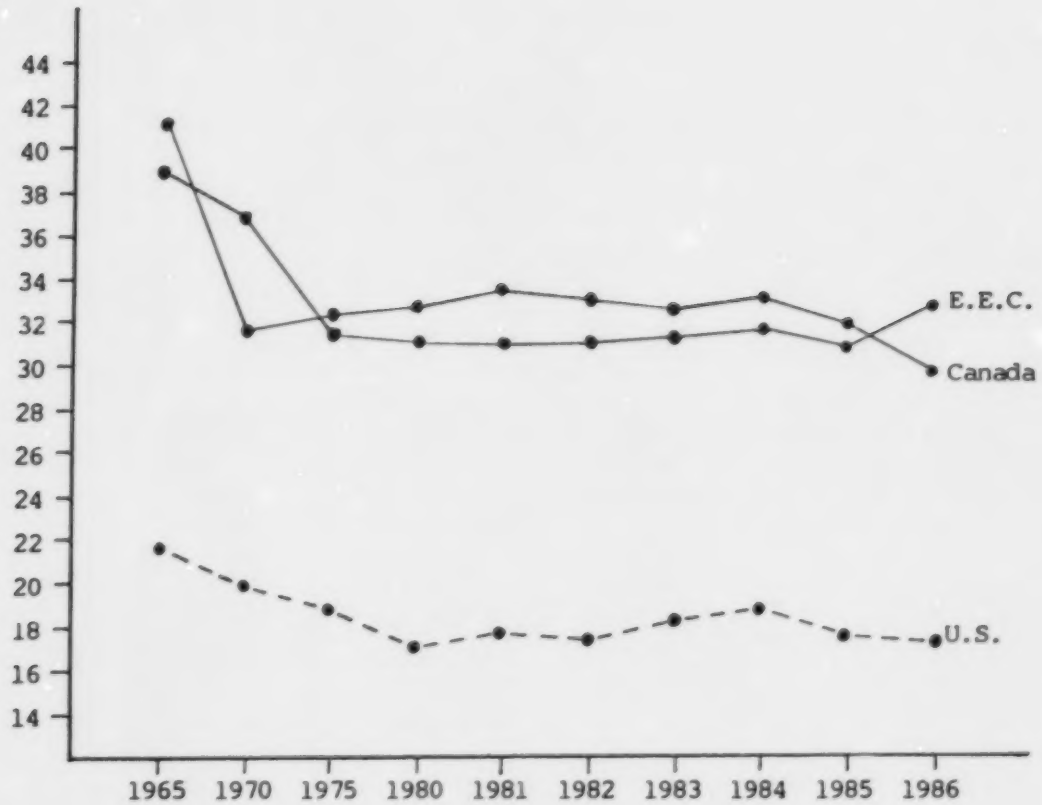


TABLE III.12

GOODS AND SERVICES TAXES AS A % OF TOTAL REVENUES 1986

Portugal	48.0%
Greece	45.4%
Ireland	44.1%
Norway	38.8%
Finland	35.8%
Denmark	35.4%
Austria	32.1%
Spain	32.0%
Turkey	31.5%
U.K.	30.9%
Australia	30.5%
Canada	29.7%
France	29.4%
New Zealand	26.9%
Netherlands	26.0%
Germany	25.2%
Sweden	24.8%
Italy	24.6%
Luxembourg	24.5%
Belgium	24.0%
Switzerland	18.8%
U.S.	17.5%
Japan	13.4%
O.E.C.D.	30.0%
E.E.C.	32.5%

TABLE III.13

WELFARE STATES AND PATTERNS OF TAXATION

	Income	Profits	Social Security	Property	Goods & Services
Sweden	38.0	4.7	25.0	2.8	24.8
Denmark	47.8	6.2	3.1	4.7	35.4
Norway	22.8	13.3	22.2	2.1	38.8
Netherlands	20.3	7.3	42.5	3.6	26.0
Belgium	33.7	6.6	33.6	1.9	24.0
Turkey	26.9	12.1	12.8	3.3	31.5
Japan	25.1	20.7	29.8	10.9	13.4
U.S.	35.4	7.0	29.8	10.3	17.5
Spain	17.7	5.9	39.1	3.2	32.0
Australia	46.6	9.0	-	8.0	30.5
O.E.C.D.	31.5	7.9	24.2	4.9	30.0
Canada	37.0	8.1	13.7	9.4	29.7

IV. PROGRESSIVE TAXATION

The SPRC supports the principle of progressive taxation and, therefore, opposes any tax reforms which would serve to increase the regressivity of current taxation.

Our support of progressive taxation is based upon concerns about the social implications of non-progressive or "flat-tax" approaches to taxation. This concern is based upon the belief that "flat-tax" systems would lead to a growth in income inequities within Canada which would eventually lead to pronounced social instability.

Insofar as high income Canadians have more opportunity to increase their incomes at a faster rate than low-income Canadians through a variety of mechanisms including investment opportunities, a progressive system of taxation is required to limit the extent to which the discrepancy between the incomes of high and low-earners can grow. It is our belief that an "unchecked" growth in this discrepancy would lead to a gap between the "haves" and "have-nots" in our society which would eventually undermine our social stability.

The only truly progressive form of personal taxation is personal income tax. Consumption taxes, property taxes and social security contributions are all "flat-taxes" and, consequently, they tend to be neutral with respect to progressivity.

A very recent study by the OECD found that Canada had the most progressive system of income tax among seventeen western industrial nations which it studied.[2] This progressivity was, in turn, largely due to a relatively generous program of allowances and relief within the income tax system for low income individuals.

It was notable that this study also found that Canada ranked second, only to the U.S., in terms of the degree of inequity in the distribution of taxable incomes. Our progressive income tax system reduced the extent of inequity, more than the American tax system, but we still ranked relatively high with respect to inequity in after-tax incomes - fourth out of the seventeen nations.

This is consistent with other statistics which indicate that an unusually high degree of income in Canada is concentrated among high income earners. (See Table IV.1). In Canada, the wealthiest 20% of the population received 7.5 times more income than the poorest 20%. Only Australia, New Zealand and France had a higher concentration of income among the wealthy. Among the eighteen industrial nations, we were tied with the U.S. for a ranking of fourth with respect to the concentration of income within the wealthiest 20% of the population. In Japan, by way of contrast, the wealthiest 20% received only 4.3

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[2]OECD, The Personal Income Tax Base. A Comparative Survey. Paris: OECD, 1990

times more income than the poorest 20%. Japan had the most equitable distribution of incomes among the eighteen countries.

It is important to note, in this regard, that the demographic structure of a country can have an effect upon income distribution. Young members of a labour force generally earn less than older members because they tend to occupy more "junior" positions. It can therefore be expected that countries with a high concentration of young adults may have a higher concentration of income earners in the lower income categories.

This trend is supported by the figures provided in Table IV.1. Four of the most inequitable countries (New Zealand, Australia, U.S. and Canada) also tend to be "young" countries from a demographic perspective.

It is also notable, however, that another "young" country - Japan - has the most equitable distribution of income while one of the older countries - France - has one of the least equitable distributions.

It is important to recognize the effects of demographic structure upon income distribution but it is equally important to recognize that demographically "young" countries (i.e., Japan) can have much more equitable distributions of income than does Canada.

It appears, therefore, that North American wage and investment structures are much more likely to concentrate wealth in the hands of high income earners than many of our European counterparts. This tendency reinforces the need for a highly progressive system of income taxation in Canada in order to counter market forces which appear to augment the "gap" between "have" and "have-nots" in North America. In other countries, with more equitable income distributions, there may be less emphasis on progressivity because of a lesser need to use taxation as a vehicle for re-distribution of income.

Clearly, the degree of progressivity needs to be addressed. In the opinion of the SPRC, the Canadian taxation system should contain a sufficient degree of progressivity to result in an after-tax distribution of incomes which, at least, reflects the "average" among Western industrial nations. Given the results of the OECD study cited earlier in this chapter, such an approach would allow for a substantial increase in the progressivity of our current taxation system.

TABLE IV.1

INCOME RATIO
Ratio of Income of the Richest 20% of the Population to the Poorest 20%
1975 to 1986

New Zealand	8.8
Australia	8.7
France	7.7
U.S.	7.5
Canada	7.5
Denmark	7.2
Italy	7.1
Norway	6.4
Finland	6.0
Switzerland	5.8
Spain	5.8
U.K.	5.7
Ireland	5.5
West German	5.0
Belgium	4.6
Netherlands	4.4
Japan	4.3

Source: The Economist Book of Vital World Statistics
N.Y. Random House, 1990.

V. PATTERNS OF TAXATION

Relative to other western industrial countries, Canada makes relatively little use of revenues from:

a) Social security contributions (Tables V.1 and V.2)

b) Taxes on financial transactions (Tables V.3 and V.4)

c) Wealth and capital transfer taxes (Table V.5)

Given the potentially progressive nature of taxation on financial transactions, wealth and capital transfer taxes, the SPRC would support increased levels of taxation in these areas.

The SPRC is concerned about an increased use of social security contributions because of the inherently "flat tax" nature of this form of taxation - all contributors pay the same rate of tax regardless of their level of income.

At present, Canada utilizes this form of taxation for unemployment insurance and the Canada Pension Plan. A previous analyses of these programs by the SPRC, indicated that the relatively low rate of revenues from this source of taxation in Canada is due to unusually low contribution rates to the pension program.[3] With respect to unemployment, the analysis indicated that Canada utilized a relatively high rate of contribution to this program, relative to other western industrial countries (See Tables V.6 and V.7).

The SPRC also recognizes that the aging of our population will require an increase in contribution levels to the CPP to bring Canada closer to the norm of most other nations. In 1987, the Canada Pension Plan act was amended to allow for an increase in the combined contribution of employees and employers from its 1991 level of 4.6% to 10.10% by 2020 and 11.68% by 2050. The National Council of Welfare has recommended improvements to the CPP which would increase rates beyond these levels.[4]

With respect to unemployment insurance, however, the SPRC is opposed to increases in contribution rates for the following reasons:

1) Canadian contribution rates are already relatively high, by international comparison.

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[3] Social Planning and Research Council of Hamilton and District. An Analysis of Social Security Contributions As a Form of Taxation. Taxation Review Task Force, Discussion Paper #3. February 1990.

[4] National Council of Welfare. Pension Reform, Ottawa: Minister of Supply and Services Canada, 1990.

2) The "flat-tax" nature of this revenue violates the SPRC commitment to progressive taxation.

3) Future increases in contribution rates should be "reserved" for the Canada Pension Plan.

The Utilization of UIC Funds:

At present, the UIC fund is utilized for the provision of benefits to unemployed workers as well as for the funding of training initiatives.

A recent Federal Commission recognized that considerable pressure is created upon the public sector in Canada to fund training initiatives because of a lack of private sector spending, relative to other industrial nations - most notably the U.S. and Japan.[5] This Commission recommended "....That the Government design and implement a flexible tax liability for firms that would be offsetting a firm's expenditures for training up to the full amount of tax".

The SPRC supports this recommendation as a measure to increase private sector funding for training in Canada. At the same time, however, we recognize that government must continue to be a partner in training endeavours because of recognized limitations in the role which can be made by the private sector:

1) Firms in older traditional sectors cannot necessarily provide training for workers in new and emerging sectors.

2) The "small" nature of the Canadian economy and the relative domination of a limited number of sectors could limit the variety of training opportunities in a diversifying economy.

3) The ability of trained labour to move from one company to another reinforces the premise that the entire burden for training cost should not rest upon individual companies.

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[5]Report of the Advisory Council on Adjustment. Adjusting to Win. Ottawa: Minister of Supplies and Services Canada, 1989.

TABLE V.1

SOCIAL SECURITY CONTRIBUTIONS
1986

	% of Total Revenues	% of GDP
France	42.7	18.9
Netherlands	42.5	19.3
Spain	39.1	11.9
Germany	37.2	14.0
Italy	34.3	12.4
Belgium	33.6	15.3
Greece	32.6	12.0
Austria	31.9	13.6
Switzerland	31.6	10.3
U.S.	29.8	8.6
Japan	29.8	8.6
Portugal	28.1	9.1
Luxembourg	25.6	10.9
Sweden	25.0	13.4
Norway	22.2	11.1
U.K.	17.9	7.0
Ireland	14.8	5.7
Canada	13.7	4.5
Turkey	12.8	2.9
Finland	9.0	3.5
Denmark	3.1	1.6
O.E.C.D.	24.2	9.3
E.E.C.	29.2	11.5

Source: Revenue Statistics of OECD Member Countries 1965-1987. Paris: OECD 1965-1987.

TABLE V.2

SOCIAL SECURITY CONTRIBUTIONS AS A % OF TOTAL REVENUES

France	42.7
Netherlands	42.5
Spain	39.1
Germany	37.2
Italy	34.3
Belgium	33.6
Greece	32.6
Austria	31.9
Switzerland	31.6
U.S.	29.8
Japan	29.8
Portugal	28.1
Luxembourg	25.6
Sweden	25.0
Norway	22.2
U.K.	17.9
Ireland	14.8
Canada	13.7
Turkey	12.8
Finland	9.0
Denmark	3.1
O.E.C.D.	24.2
E.E.C.	29.2

Source: ibid.

TABLE V.3

TAXATION ON FINANCIAL AND CAPITAL TRANSACTIONS
AS A % OF G.D.P.
1985

	As a % of GDP	Additional* Revenues
Switzerland	1.01	4842.7
Australia	.92	4554.9
Finland	.82	3931.6
Italy	.79	3787.8
Japan	.79	3787.8
Luxembourg	.73	3500.1
Denmark	.73	3500.1
Spain	.54	2589.1
France	.53	2541.2
Belgium	.51	2445.2
Sweden	.38	1821.9
Netherlands	.33	1582.2
U.K.	.33	1582.2
New Zealand	.29	958.9
Germany	.24	1150.7
Austria	.24	1150.7
Norway	.13	1438.4
U.S.	.04	191.8
Canada	0	

*The amount of additional revenues that would have been generated in Canada in 1985. (Millions of dollars)

G.D.P. 1985 - 479,446 million

Source: ibid.

TABLE V.4

TAXATION ON FINANCIAL AND CAPITAL TRANSACTIONS
AS A % OF TOTAL TAXATION REVENUES
1985

Switzerland	3.14
Australia	3.02
Japan	2.83
Italy	2.29
Finland	2.20
Luxembourg	1.71
Denmark	1.48
France	1.16
Belgium	1.09
U.K.	.87
New Zealand	.84
Sweden	.76
Netherlands	.74
Germany	.64
Austria	.56
Norway	.27
U.S.	.14
Canada	0

Source: ibid.

TABLE V.5

COMBINED REVENUE FROM NET WEALTH TAXES ON INDIVIDUALS AND CAPITAL TRANSFER TAXES AS A % OF TOTAL REVENUES
1985

Switzerland	3.06
Japan	1.19
Greece	.94
Netherlands	.94
Denmark	.92
France	.85
Portugal	.83
U.S.	.77
Sweden	.68
U.K.	.64
Norway	.61
Belgium	.58
Austria	.51
Luxembourg	.51
Finland	.50
Spain	.49
Germany	.42
Ireland	.30
Italy	.23
New Zealand	.19
Turkey	.19
Canada	.03
Australia	.01

Source: ibid.

TABLE V.6

EMPLOYER AND EMPLOYEE CONTRIBUTION
RATES TO PUBLIC PENSION PLANS
1987

	Employer*	Employee**
Sweden	19.65	.0
Finland	17.0	1.8
Italy	17.0	7.15
Austria	10.25	10.2
Germany	9.35	9.3
France	8.2	6.4
Luxembourg	8.0	8.0
Japan	6.2	6.2
Netherlands	6.0	27.0
USA	5.7	5.7
Switzerland	4.2	4.7
Canada	1.9	1.9

* % of Payroll ** % of Earnings

Source: U.S. Department of Health and Human Services
Research Report #61. Social Security Programs
Throughout the World, 1987.

TABLE V.7

EMPLOYER AND EMPLOYEE CONTRIBUTION RATES TO UNEMPLOYMENT COMPENSATION 1987

	Employer*	Employee**
USA	6.2	.0
France	4.3	2.31
Canada	3.3	2.35
Sweden	2.2	.0
Austria	2.2	2.2
Germany	2.1	2.15
Italy	1.6	.0
Netherlands	1.3	1.28
Japan	.9	.55
Switzerland	.3	.30
Luxembourg	.0	5.0
	* % of Payroll	** % of Earnings

Note: Norway and UK include unemployment contributions as part of a general social security tax which also includes health insurance, pensions and workmen's compensation. In UK, the rate was 5% to 10% depending on the employee's wage level and in Norway, employers contributed 17% of Payroll.

Source: US Department of Health and Human Services, Research Report # 61, Social Security Programs Throughout the World, 1987.

VI. CORPORATE TAXATION

One of the more controversial areas of the taxation debate in Canada, relates to the decreasing contribution of taxes on corporate profits to tax revenues. A review of international trends, however, indicates that this decreased dependence of corporate profit taxation reflects a general trend which brings North American patterns in line with European patterns (see Chapter III).

Canada exhibits a somewhat high dependence on this revenue source (Table VI.1) but this is more than offset by a more limited use of employer social security contributions (Table VI.2). When these two revenue sources are combined, Canada's use of corporate taxation revenues are moderately low. (Tables VI.3 and VI.4). It should be recognized, however, that employer social security contributions in Canada will rise with the planned implementation of increased contribution rates for the Canada Pension Plan (See Chapter V Patterns of Taxation).

Despite Canada's somewhat higher than average use of corporate profit taxation, the general rates of taxation on corporate profits is relatively low in Canada. A 1988 review of recent changes in corporate taxation rates by the OECD reported the following base rates for eleven of their member nations[6]:

West Germany	50% (retained profits)
Japan	42%
France	42%
Australia	39%
U.K.	35%
Netherlands	35%
Portugal	35%
U.S.	34%
Austria	30%
Canada	28%
Finland	28%

It should be noted that international comparisons between corporate taxation rates are complicated by a number of factors -

1. Inadequate data related to corporate taxation levied through property taxes.

2. The use of differential tax rates for different corporate sectors.

3. Tax expenditure programs which result in special tax-relief for specific activities which are sometimes of a time-limited nature.

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[6] A Birds Eye View of Corporate Tax Reforms, OECD Observer, January 1989.

4. The partial integration of corporate and personal taxation in some countries.

In any discussion of corporate taxation, the issue of international competitiveness moves to the forefront. The international competitiveness of Canadian industries can be hurt, to the extent that production costs are increased in Canada; beyond that of other nations, by corporate taxation rates. A recent article in Canadian Business reviewed the current status of Canadian corporate taxation, relative to that of our major competitors, and came to the following conclusion -

> "No matter what comparison you use - statutory rates, average rates, METRs - it is simply untrue to say that Canada's corporate tax system is seriously hurting Canadian competitiveness, however that is defined. But neither is it true that business is getting a free ride. Canadian companies pay about the same rate as individuals, and tax reform has closed many of the loopholes that formerly eroded the corporate tax base. (pg. 62)"[7]

In general, therefore, it does not appear that current corporate taxation rates in Canada are injurious to international competitiveness.

Elsewhere in this report, a number of recommendations have been made relative to corporate taxation -

1) The introduction of a special tax for training purposes.

2) The review of a broad-based speculation tax.

3) The decreased utilization of tax expenditure programs.

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[7] Coyne, A. Taxing Question. Canadian Business, January 1991, ('59-62).

TABLE VI.1

TAXES ON CORPORATE INCOME (1988)

	% of Total Taxation Revenues	% of GDP
Japan	20.7	6.0
Luxembourg	16.7	7.1
Norway	13.3	6.6
Turkey	12.1	2.7
U.K.	10.3	4.0
Australia	9.0	2.8
Canada	8.1	2.7
Netherlands	7.3	3.3
New Zealand	7.0	2.3
U.S.	7.0	2.0
Belgium	6.6	3.0
Switzerland	6.2	2.0
Denmark	6.2	3.1
Germany	6.0	2.2
Spain	5.9	1.8
France	5.1	2.3
Sweden	4.7	2.5
Greece	4.0	1.4
Finland	3.7	1.4
Ireland	3.5	1.4
Austria	3.4	1.4
O.E.C.D.	7.9	3.0
E.E.C.	7.2	3.0

TABLE VI.2

EMPLOYERS' SOCIAL SECURITY CONTRIBUTIONS AS A PERCENTAGE OF TOTAL TAXATION

1986

Spain	29.4
France	27.4
Italy	24.6
Sweden	24.1
Germany	19.1
Portugal	18.5
Netherlands	17.3
Belgium	17.3
U.S.	17.3
Austria	15.8
Japan	15.4
Norway	14.9
Greece	14.3
Luxembourg	13.8
Switzerland	9.9
U.K.	9.1
Ireland	9.1
Finland	9.0
Canada	8.7
Turkey	7.5
Denmark	1.2
Average	15.4

TABLE VI.3

CORPORATE INCOME TAX AND EMPLOYER SOCIAL SECURITY CONTRIBUTIONS AS A % OF TOTAL REVENUES

Japan	36.0
Spain	35.3
France	32.5
Luxembourg	30.4
Italy	29.4
Sweden	28.8
Norway	28.2
Germany	25.0
Netherlands	24.6
U.S.	24.2
Belgium	23.8
Turkey	19.6
U.K.	19.4
Austria	19.2
Greece	18.2
Switzerland	17.2
Canada	16.8
Finland	12.8
Ireland	12.6
Australia	9.0
Denmark	7.4
New Zealand	7.0

TABLE VI.4

TAXES ON CORPORATE INCOME AND EMPLOYER SOCIAL SECURITY CONTRIBUTIONS AS A % OF GDP

1986

Sweden	15.4
France	14.4
Norway	14.0
Luxembourg	13.0
Italy	12.1
Netherlands	11.2
Belgium	10.8
Spain	10.7
Japan	10.4
Germany	9.4
Austria	8.1
U.K.	7.6
U.S.	7.0
Greece	6.6
Canada	5.8
Switzerland	5.2
Ireland	5.1
Finland	4.9
Turkey	4.4
Denmark	3.7
Australia	2.8
New Zealand	2.3
Average	8.4

VII. TAXATION ON SPECULATION

The SPRC recognizes the critical importance of investment funds to the future economic health of the country. It also recognizes that taxation policies have significant impacts upon the flow of these funds. Investment dollars go to investments which promise the greatest rates of return and patterns of taxation can have dramatic affects upon returns on investment.

At the same time, the SPRC recognizes that sectors which provide the greatest rate of return are sometimes of limited relevance to the achievement of critical national economic and social goals pertaining to competitiveness, employment and equity.

For example, the recent inflation in property values have provided dramatic rates of return for investors but have contributed relatively little to national economic and social goals. The broader consequences of this inflation have been largely negative:

1) A reduction in the amount of investment funds available for other more productive activities as more funds are diverted to real estate speculation.

2) Renewed concerns about general inflationary pressures which, in turn, have resulted in a tight-money policy and a general slow-down in the economy.

3) An affordable housing crisis which has threatened the basic shelter needs of lower income Canadians.

4) An increase in government expenditures due to increased shelter allowances and construction of non-profit housing.

The SPRC is, therefore, in favour of a real-estate based speculation tax which would:

1) Lower the rates of return which accrue from short-term speculation in the real-estate market and, consequently, decrease the attractiveness of land speculation in order to "free-up" investment funds for other more productive use, and,

2) Offset the public sector costs which are the inevitable consequence of escalating land prices.

The SPRC also believes that the use of a graduated tax, based upon the length of time that an investment is held, should be investigated in other areas of investment activity. Higher rates of taxation on returns from investments which are short-term in nature could have the effect of increasing the flow of investment dollars to important initiatives which involve lower short-term, but higher, long-term returns. Such an approach to taxation would provide an

incentive for directing capital and talent into areas of activity which could foster the long-term creation of wealth to a far greater extent than occurs under current tax structures. The primary objective of a graduated tax on speculation should not be one of revenue generation but, rather, the re-direction of investment funds away from short-term returns that contribute relatively little to the ongoing economic health of the nation.

The need for a tax-based control of short-term speculation in Canada is augmented by the unique characteristics of industrial financing in North America. According to recent analyses, North American companies rely to a much greater degree on equity financing and to a much lesser degree on debt financing than their European and Japanese counterparts.[8] This dependence upon market financing can create greater pressure for short-term returns which can involve the making of sacrifices with respect to longer-term growth and stability.

The argument for a broad-based speculation tax was made, in a somewhat humorous manner, by Chrysler CEO, Lee Iacocca in a 1987 speech to a conference of Magazine Publishers and Editors -

> "Another example of short-term thinking: We held a management meeting at Chrysler in July and word leaked out that we were considering a "restructuring" . . . Wall Street figured we must be going to sell something off and a big wad of dough would go into immediate earnings.
>
> So our stock shot up almost 10 percent in one day - just on a rumour. But after the meeting was over and it was clear that we were not going to tear the company apart that we were only going to reduce our cost structure a billion dollars (the old fashioned way) - it wasn't exciting enough. So the stock dropped 10 percent the next day!
>
> It's crazy, but the whole country seems to be in a short-term feeding frenzy - make a quick buck and get out, look out for yourself, live for today . . .
>
> How about a 40 percent tax on assets held less than 90 days, 28 percent up to two years, 15 percent up to five years and after that the tax rate goes to zero . . . Do you think that might make investors take a longer view? Do you think more companies would be building research and development centres if they didn't pay a penalty in their stock price for investing in such long-term assets?"

The SPRC recognizes that problems would exist in the design and implementation of such a broad-based taxation on speculation. At the same time, however, we believe that this option should be given serious study. Every form of taxation involves both positive and negative impacts. Given the potential benefits of a broad-based speculation tax with respect to the longer-term economic health of Canada, it is possible that the advantages of such a form of taxation would outweigh the disadvantages.

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[8]Kuttner, R. The Economic Illusion, N.Y. Houghton Mifflin Co., 1984.

VIII. TAX EXPENDITURES

"Tax expenditures" refer to taxation revenues which are foregone by government for the purpose of reducing the tax-load in some areas of the economy. The most common use of tax expenditures are in the form of special low tax rates for investments in targeted undertakings - i.e. research and development, movies, multiple-dwellings, etc.

The importance of tax expenditures in Canada was first identified in the 1976 report of the National Council on Welfare, entitled "The Hidden Welfare System". Following the publication of that report, the Federal Government began a more accurate accounting and reporting of tax expenditures and, as a result, Canada has one of the most comprehensive reporting systems on tax expenditures in the Western World.[9]

In the early 1980's, tax expenditures by the Federal Government amounted to 36 billion dollars per year.[10]

Unfortunately, international comparisons of tax expenditures are not possible because of inadequate accounting and reporting systems in many nations.[11]

One of the key problems with tax expenditures was outlined by Auditor General Kenneth Dye, in his 1985 report -

> "A cost-conscious Parliament is in the position of a team of engineers trying to design a more fuel-efficient automobile. They think they have succeeded, but the engine seems to go on consuming as much gas as it did before. They cannot understand the problem until they notice that, hidden from view, myriad small holes have been punched through the bottom of the gas tank. This is too often the way of tax expenditure. Revenue leaks away, and MPs do not know about it until it is too late."[12]

A recent analysis by Kuttner (1984), however, concluded that tax expenditures are used to a much greater degree in North America, than in Europe or Japan. In West Germany and Japan, for example, there are virtually no tax expenditures. In fact, those two countries do not even allow for accelerated depreciation of corporate assets.

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9 Tax Expenditures: A Review of the Issues and Country Practices. Paris: OECD. 1984.

10 Canada: Department of Finance. Government of Canada Tax Expenditure Account. Ottawa: 1983

11 OECD ibid.

12 Canada. Report of the Auditor General of Canada to the House of Commons. Ottawa: 1985.

During the past few years, the use of tax expenditures in Canada has been reduced. This has occurred, to a considerable extent, because of concerns about the effectiveness of tax expenditures as a vehicle for increasing productive investment. Two very large tax expenditure programs (MURBS and the Research and Development Tax Credit) were notable for their failure to achieve their desired objectives.

One of the primary purposes of tax expenditures is to provide tax relief to specific sectors of the economy which, for a variety of reasons, are judged to require the economic impetus of increased retained profits. The primary criticism of this approach to national economic planning relates to the relative "invisibility" of these foregone revenues with respect to public accountability. Critics argue that the same purpose could be served by direct subsidies through loans or grants to the relevant enterprise. Insofar as specific loans or grants can be more readily "attached" to specific actions by the recipient organization, accountability for the use of public funds is enhanced.

For the reasons cited above, the SPRC does not support the use of tax expenditures as an instrument of economic policy. The SPRC, therefore, supports the current trend to reduce the use of tax expenditures by all levels of government.

IX. EXPENDITURE PATTERNS

National accounting systems utilize two summary measure of government expenditures - total outlays and current disbursements. "Total outlays" includes all expenditures made by government during a given year. "Current disbursements" includes all expenditures, with the exception of gross capital formation and the purchase of land or other intangible assets. It, therefore, represents all expenditures for which there was not a corresponding increase in assets on the government balance sheet.

Expenditures by all levels of government in these two areas as a percent of Gross Domestic Product (GDP) for 16 nations in 1986 are presented in Table IX.1. With respect to total outlays, Canada and the U.K. ranked 9th, 6 points above the OECD average and 2 points below the average for the European Economic Community (EEC).

Canada ranked 10th on current disbursements, 5 points above the OECD average and 1.5 points below the EEC average. In general, the traditional welfare states ranked highest while the free-market economics of the U.S., Switzerland and Japan had the lowest rates of expenditure. Canada occupied a mid-point between these extremes.

Reliable comparative data on specific programs is not readily available from one source. Our analysis on program expenditures, therefore, utilized the best available data on comparative expenditures in four areas of program activity - social security, labour market programs, health, and education.

Social Security Expenditures

Within the OECD accounting system, "social security expenditures" include all programs which provide persons with incomes - "social security benefits for sickness, old age, family allowances, etc., social assistance grants and unfunded employee welfare benefits paid by general government".

As presented in Table IX.2, Canada ranked relatively low, among OECD nations, in terms of social security expenditures as a percent of GDP. Part of the reason for this lower than average ranking, relates to the demographics of Canada - the largest part of the "social-security bill" in most countries is pensions and Canada has a relatively low concentration of persons aged sixty-five and over (See Table IX.2).

Employment Related Programs

Table IX.3 presents 1987 spending levels for 22 nations on labour market programs. The two primary components of this group of programs are training and income maintenance. Unemployment rates are also presented to allow for an examination of the relationship between unemployment and labour market spending.

With respect to spending, Canada ranked 11th, only .01 point above the average for the 22 countries. In terms of unemployment, Canada ranked 8th, 1.3 points above average.

To further examine the relationship between spending and unemployment, ratios were calculated by dividing the expenditure rate by the unemployment rate. The resulting ratio indicates the percentage of GDP which each country spends on labour market programs for each point in their unemployment rate. At the high end, then, Sweden spends .98% of its GDP for every point of its unemployment rate. At the low end, Portugal and Italy spend only .11% of their GDP for every point of unemployment.

The average ratio, among the 21 nations was .33. The Canadian ration was .23. It appeared, therefore, that Canada spent somewhat less than average for every point of unemployment it experienced. As a result of "ties" between countries, the 23 nations occupied 17 ranks and Canada ranked 10th.

The countries which spent the most, relative to their levels of unemployment, were Sweden, Denmark, Switzerland, Finland, and New Zealand. The countries which spent the least were Portugal, Italy, U.S., Greece, and Spain.

Educational Spending

As presented in Table IX.4, Canada ranked second among major western industrial nations with respect to government expenditures on education, as a percent of GDP, for the year 1983. These figures include spending by all levels of government.

To some extent, this spending appeared to be related to the demographic structure of the Canadian population - Canada ranked third in terms of the proportion of its population that was aged 0 to 14 and second with respect to the number of students in post-secondary educational institutions per 100,000 population. It is noteworthy, however, that we ranked considerably lower (10/15) in terms of the proportions of 17 year olds who are enrolled in educational institutions. This suggests that Canada is somewhat unique in terms of containing a relatively high rate of enrolment in post-secondary institutions while, at the same time, possessing a relatively high "drop-cut" rate among secondary school students.

Health

The mix of private and public funding in national health expenditures is presented in Figure IX.5. In terms of total spending, Canada ranked third behind the U.S. and Sweden. With respect to the government portion of the cost, Canada ranked 7th among the 21 nations. All OECD nations, with the exception of the U.S., have some form of universal national health insurance in place.

One of the primary determinants of the demand for health care in nations is the size of the population group aged 65 or over and the number of newborns. As

presented below, however, Canada experienced an "average" birthrate and a relatively low concentration of seniors, relative to the other OECD nations. Neither of these factors, therefore, appear to account for the higher than average expenditure on health care in Canada.

Table IX.6 provides comparative data pertaining to the supply of health services within the population. With respect to the number of doctors and nurses per million population, Canada ranks low (15/22 and 16/18 respectively) among the OECD nations for which data was available. We were very close to the OECD average with respect to hospital beds. It is notable, however, that we ranked first with respect to the proportion of our elderly population residing in "institutions".

In general, then, Canada reported a higher than average expenditure on health care, despite average birth rates and a relatively low concentration of senior citizens. This did not appear to be due to an "over supply" of physicians, nurses, or hospital beds, although we did report an unusually high rate of "institutionalization" of our elderly population.

Conclusions

With respect to general expenditures, Canada tended to occupy a mid-point rank between European nations and traditional free-market economies, such as the U.S. Some variation did occur, however, with respect to specific program areas. We ranked relatively high in expenditures on health and education, we were in the "average" range of spending on labour market programs and at the low end of spending on social security.

TABLE IX.1

General Government Expenditures
1986

Country	Total Outlays As A % of GDP 1986	Current Disbursements As A % of GDP 1986
Sweden	63.5	59.9
Netherlands	59.1	54.0
Denmark	55.4	53.3
Belgium	53.2	51.4
France	52.4	49.4
Norway	41.0	47.6
Austria	51.9	46.3
Italy	50.5	45.6
Germany	46.6	42.9
U.K.	46.2	43.3
Canada	46.2	43.0
Greece	42.8	42.8
Finland	42.3	38.7
Spain	42.2	36.8
U.S.	36.9	35.6
Japan	33.1	27.4
Switzerland	30.4	30.4
EEC	48.3	44.5
OECD	40.2	37.1

Current disbursements consists mainly of final consumption expenditures, interest on debt, subsidies and social security transfers.

Total outlays consist of current disbursements plus gross capital formation and purchases of land and intangible assets.

Source: Historical Statistics 1960 -1986.
Paris, OECD, 1988.

TABLE IX.2

Social Security and
The Aging Population

Country	Social Security Transfers as a % of GDP 1986[1]	Population Aged 65 and Over 1990[2]
France	26.4	13.8
Netherlands	25.9	12.7
Belgium	21.2	14.2
Austria	20.3	14.6
Italy	17.2	13.8
Spain	16.6	12.7
Germany	15.8	15.5
Norway	15.8	16.2
Denmark	15.5	15.3
Greece	14.6	12.3
U.K.	14.1	15.1
Switzerland	13.7	14.8
Canada	12.3	11.4
Japan	11.4	11.4
Finland	11.1	13.1
U.S A.	11.0	12.2
Iceland	4.6	10.3
OECD Average	13.0	13.0
EEC Average	16.7	N.A

Sources: [1] Historical Statistics 1960 -1986.
Paris, OECD, 1987
[2] Maguire, M. Making Provisions for An
Aging Population.
OECD Observer, No. 148.
Oct/Nov 1987 (4-7).

TABLE IX.3

Labour Market Expenditures and Unemployment

Country	Expenditure on All Labour Market Programs % of GDP[1] 1987	Unemployment Rate[2]	Ratio[3]	Ratio Rank
Ireland	5.12	17.4	.29	9
Denmark	5.03	5.5	.91	2
Belgium	4.35	11.3	.40	6
Netherlands	3.99	10.4	.38	7
Spain	3.30	21.0	.15	14
France	3.07	10.4	.29	9
Sweden	2.66	2.7	.98	1
U. K.	2.57	11.6	.22	11
Finland	2.39	5.3	.45	4
Germany	2.34	8.0	.29	9
Canada	2.24	9.5	.23	10
New Zealand	1.72	4.0	.43	5
Australia	1.53	7.8	.19	13
Luxembourg	1.51		N.A	
Austria	1.48	4.5	.32	8
Italy	1.27	10.9	.11	17
Greece	.98	7.4	.13	15
Portugal	.94	8.0	.11	17
U.S.	.83	6.4	.12	16
Norway	.76	2.0	.38	7
Japan	.59	2.8	.21	12
Switzerland	.40	0.8	.50	3
Average	2.23	8.2	.33	

1 OECD Statistics presented in Quarterly Labour Market and Productivity Review, Spring 1989. Canadian Labour Market Productivity Centre.

2 Historical Statistics, OECD, 1989.

3 The percent of GDP which each country spends on labour market programs for each point of their unemployment rate.

TABLE IX.4

Educational Spending and Demand Factors

	Education As A % of GDP[1]	Population 0 - 14 [2]	No. Students/ 100,000 Third Level [3]	Enrolment of 17 Yr. Olds % [3]
Sweden	7.7	17.5	2,635	85
Canada	7.0	21.5	4,853	76
Netherlands	6.9	19.5	2,795	86
U.S.	6.7	21.7	5,167	88
Ireland	6.7	29.7	1,888	
Norway	6.5	20.4	2,124	75
Denmark	6.4	18.7	2,271	74
Belgium	6.1	19.0	2,546	86
France	6.1	21.2	2,358	75
Austria	5.8	18.6	2,398	78
Finland	5.8	19.4	2,733	
Luxembourg	5.2	17.3	232	
U. K.	5.2	19.2	1,806	65
Japan	5.1	21.5	1,987	90
Switzerland	4.8	16.9	1,789	82
Germany	4.6	15.6	2,596	97
Portugal	4.6	23.5	1,112	41
Italy	4.0	19.6	1,989	70

1 UNESCO Yearbook, 1986.

2 United Nations Statistical Yearbook, 1986.

3 Reutersward, A., Educating and Training Tomorrow's Workforce, OECD Observer, December 1987/January 1988.

FIGURE IX.5
HEALTH EXPENDITURE AS % OF GDP 1987

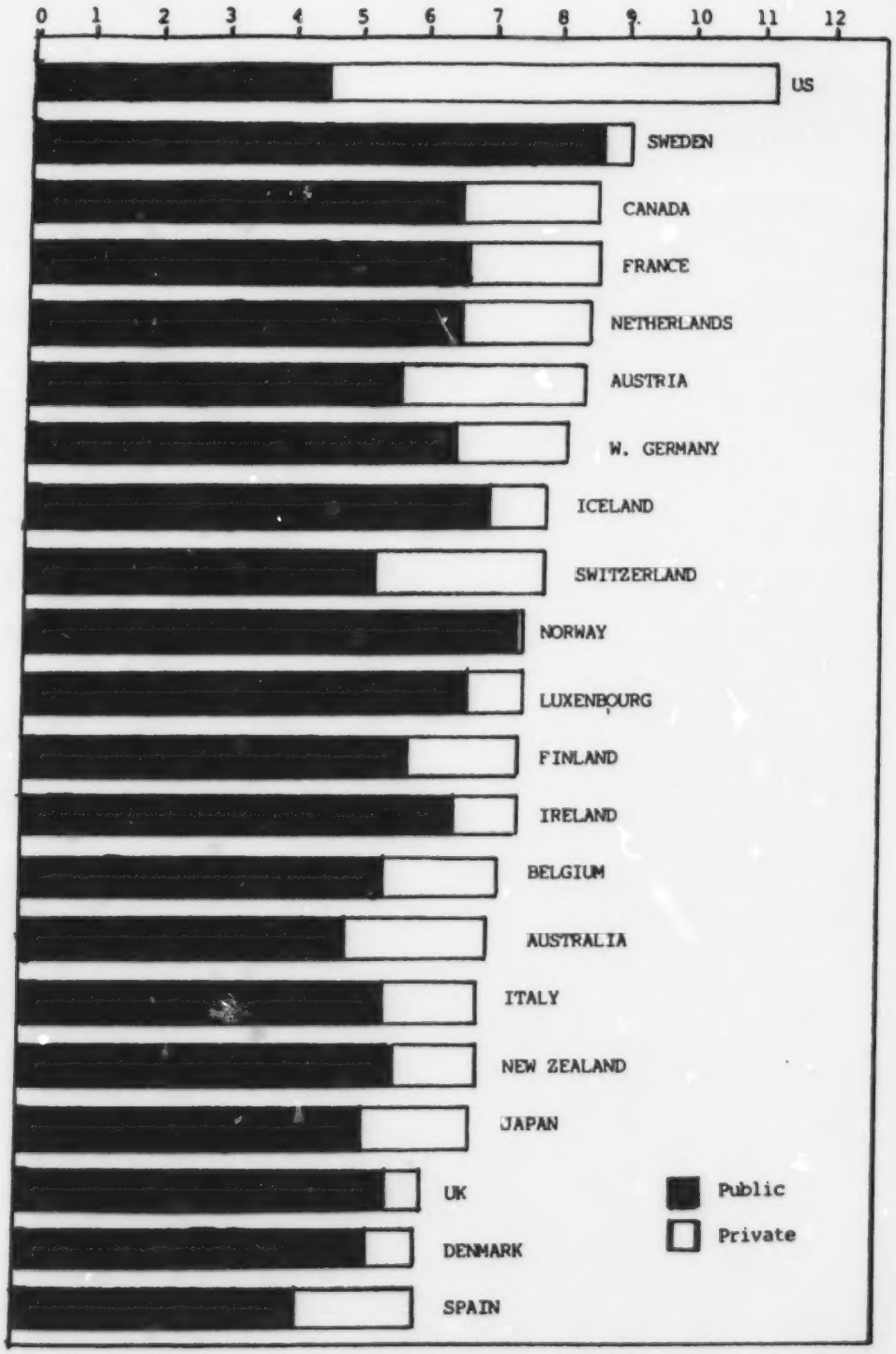

TABLE IX.6

Health Services: Supply

Doctors/ Million[1] People (1983-88)		Hospital Beds/[1] 1000 Population		% Population 75+ in[2] Institutions 1980-81		Nurses/Million[1]	
Italy	4267	Finland	14.9	Canada	17.5	New Zealand	12,447
Spain	3547	Sweden	13.2	Denmark	13.4	Finland	8,724
Belgium	3119	France	12.9	Norway	11.0	Norway	8,465
Austria	3008	Netherlands	12.0	France	9.1	Australia	8,435
Greece	2907	Japan	11.8	Sweden	7.8	U.S.A.	7,891
Sweden	2743	Switzerland	11.3	U.K.	7.8	Switzerland	7,719
West Germany	2696	West Germany	11.0	Austria	7.3	Sweden	7,635
Denmark	2567	Austria	10.4	Germany	7.4	Ireland	7,136
Portugal	2534	Belgium	8.9	Japan	5.8	Denmark	5,994
Netherlands	2517	U.K.	8.0			Austria	5,618
France	2485	Italy	7.8			Japan	5,315
Norway	2248	Canada(12/20)	7.6			France	5,267
Finland	2237	New Zealand	7.3			West Germany	5,149
Australia	2215	Denmark	6.9			Italy	3,952
U.S.A.	2035	U.S.A.	5.9			Spain	3,809
Canada(16/22)	1883	Norway	5.8			Canada(16/18)	3,296
Luxembourg	1800	Ireland	5.3			U.K.	3,204
New Zealand	1747	Greece	5.2			Belgium	968
U.K.	1615	Spain	5.1				
Switzerland	1602	Greece	5.2				
Ireland	1463						
Japan	1477						

Sources: [1] Economist, Book of Vital World Statistics. London, The Economist Books Ltd., 1990.

[2] United Nations Demographic Yearbook, 1987.

X. THE CANADIAN DEFICIT

Current debates concerning deficits and taxation in Canada are illustrative of the classical "Canadian Conundrum".

As a nation, we want to provide "European style" social programs, using "American style" taxation. We have attempted to resolve this problem by developing social programs which are less generous than their European counterparts and taxation policies which generate somewhat more revenue than in the U.S.

To a considerable extent, we have been remarkably successful in achieving this balance. The degree of our success is evidenced in two statistical indicators which have been developed by statisticians at the United Nations to monitor the "wealth" and "welfare" of member nations. The first of these, the Purchasing Power Parity Index, is a measure of the wealth of nations which takes into account the size of the GDP per capita and the cost-of-living in different countries. The index is calculated such that it is equal to 100 for the U.S.

As presented in Table X.1, Canada ranks second to the U.S. on this measure. In terms of the goods and services which can be purchased with our wealth, Canada ranked as the second wealthiest nation among the western industrial grouping.

The second measure is the Human Development Index. This is a new indicator, developed by the UN, to combine elements of health, education, and poverty into one measure of "human development". It combines measures of life expectancy, literacy, and the extent to which average income, based on purchasing power parity ratios, is sufficient to meet basic needs. As presented on Table IX.1, Canada also ranked high, on this measure, among OECD member nations - we were tied with Norway for a fifth place ranking among the 22 nations.

Most noticeably only Turkey and Portugal scored lower than the U.S. on this measure. It is striking that the U.S. ranked so low on the human development index, despite ranking first on the PPP measure of individual wealth.

TABLE X.1

Wealth, Welfare and Taxation Burdens

	P.P.P.[1] 1989	Human[1] Development Index 1989	Tax[2] Burden 1986
U.S.	100	96.1	28.9
Canada	92.5	98.3	33.2
Switzerland	87.0	98.6	32.6
Norway	84.4	98.3	49.8
Luxembourg	79.0	-	42.4
Iceland	79.0	-	-
Sweden	76.9	98.7	53.5
Denmark	74.2	97.1	50.6
West Germany	73.8	96.7	37.5
Japan	71.5	99.6	28.8
Australia	71.1	97.8	31.4
Finland	69.5	96.7	38.4
France	69.3	97.4	44.2
Netherlands	68.2	98.4	45.5
U.K.	66.1	97.0	39.0
Austria	66.1	96.1	42.6
Italy	65.6	96.6	36.2
Belgium	64.7	96.6	45.4
New Zealand	60.9	96.6	32.9
Spain	46.0	96.5	30.4
Ireland	40.9	96.1	-
Greece	36.0	-	36.7
Portugal	33.8	-	32.4
Turkey	21.8	-	22.7

Sources:

1. The Economist Book of Vital Statistics, N.Y: Random House, 1990

2. Revenue Statistics of OECD Member Countries, Paris: OECD, 1988

Table X.1 also presents the "tax burden" for these countries. From these combined analyses, it appears that Canada and Switzerland are unique among western industrial nations with respect to maintaining high levels of individual wealth and human development, with relatively low tax-burdens.

The contrast between Canada and the U.S. is worthy of further comment. Both countries have high levels of individual wealth and relatively low levels of tax-burden. Canada, however, ranks much higher on the human development index and this is probably due to the higher levels of government expenditure in Canada, particularly in important areas of health, labour force and social services.

The balance which we have struck between "European Style" programs and "American Style" taxation has proven, therefore, to be relatively successful. We have managed to achieve this goal, however, through the development of a large government deficit, by international standards, as we attempt to fund government programs through borrowing rather than increased taxation.

It must also be recognized that meaningful international comparisons between government debts are made difficult by differing balances of public/private enterprise in different countries. This is particularly true of Canada and the United States.

In the U.S., for example, most utilities are privately owned. Consequently, the extensive borrowing which is done by these utilities is not part of the public sector debt in the United States. In Canada, however, most utilities are within the public sector and the government borrows on behalf of these Crown Corporations. This tends to "inflate" the public sector debt in Canada, relative to the U.S., despite the fact that both of these sources create pressures upon capital markets. The capital markets are affected equally, regardless of whether the borrower is from the private or public sector.

The same factors apply to the much higher levels of private ownership in the American hospital and education systems. When the Hospital Corporation of America borrows money for the purpose of building a new hospital, it creates pressures upon the capital market which are indistinct from the pressure of a government which is borrowing for the purpose of hospital construction.

Any meaningful comparison of public sector debts between the U.S. and Canada should take into account the different balances of public/private enterprise within the two countries.

It is generally recognized, however, that the size of the federal deficit in Canada has reached unacceptable proportions due to the dramatic increase that occurred during the 1980's.

The citizens of Canada are, therefore, faced with the following choices as a means for decreasing the size of the deficit:

1) Decreasing expenditures to bring Canadian programs in line with American counterparts.

2) Increasing taxation to bring the taxation burden more in line with our European counterparts.

The experience of other nations during the past two decades indicates that increased taxation burdens could be implemented without negative effects upon the economy.[13]

The choice of the mix of these two options is, therefore, primarily one of philosophical and moral consideration. The resolution of our conundrum ultimately comes down to the question of - how much of their income are Canadians willing to "throw into the government pot".

Europeans throw in considerably more than Canadians and are, consequently, able to maintain more generous programs with lower levels of borrowing. Americans put less of their national wealth into government coffers and, consequently, have much more limited programs.

The SPRC is very concerned that, during the past decade, this fundamental question has been addressed in a piecemeal fashion through apparently unrelated budget measures, with a minimum of public discussion about the fundamental principles which underlie these measures.

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[13] Social Planning and Research Council of Hamilton and District Taxation Burdens and Economic Growth. International Comparisons. Discussion Paper No. 8. Taxation Review Task Force, June 1990.

XI. THE AMERICAN PRESENCE

One of the central quandaries of Canadian tax policies relates to our geographical and economic proximity to the U.S. The U.S. is our major trading partner - over 70% of our exports are destined to that market and this high degree of dependency is unique among western industrial nations - no other OECD member nation depends on one other country for more than 35% of its export market.[14]

This fact of life creates considerable pressure for Canadian companies to keep production costs at comparative levels to the U.S. or face the problem of "pricing" themselves out of the U.S. market. To the extent that tax-burdens are a cost-of-production, the proximity of Canada to the U.S. creates pressures to keep our tax-burden close to that of the U.S.

Concerns about a potential "brain drain" of talented Canadians to the U.S. are also used to justify the need to keep personal taxes at relatively comparable levels.

Among Western industrial nations, the U.S. has one of the lowest tax-burdens and levels of government expenditure and our proximity to the U.S. creates an ongoing "downward pull" on both taxation and expenditures in Canada. The U.S. also has one of the most limited social support systems among western industrial countries and, as a result, Canadian social policy advocates fight an ongoing battle to prevent the development of a "level playing field" between the two countries with respect to social supports.

The limited nature of American social support systems was graphically obvious in a 1990 issue of Newsweek which was devoted to the topic of the American family.[15] In that issue, the editors lamented the condition of the American family and proposed a six-point "radical" agenda to rescue the American family from its current malaise. Notably, the editors believed that this agenda would be politically unacceptable. Their "radical" agenda was composed of the following items - family allowances, guaranteed maternity leave protection, pay equity for working women, cash payments to mothers for wages lost during maternity leave, full health care insurance for all children, and national standards on day care. Four of these programs are "standard" programs in Canada - family allowances, maternity leave payments/protection and health insurance. In fact, the U.S. is the only OECD member nation, with the exception of Turkey, which does not have family allowances and a universal health insurance plan.

With respect to social policy, then, the U.S. does not represent the "norm" among western industrial nations - it is the exception. It has one of the most limited social safety nets in the western world.

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[14] The Economist, Book of Vital World Statistics. London: The Economist Books Ltd., 1990.

[15] Newsweek Special Edition. The 21st Century Family. Winter/Spring, 1990

Table XI.1 provides a comparison between Canada and the United States on key dimensions of social stability, health status and economic performance. The inescapable conclusion from these figures is that Canada has managed to maintain a more healthy population and greater social stability with no sacrifice in economic performance. It is equally important to note that the U.S. has one of the highest poverty rates, maternal/infant mortality rates and the highest divorce and murder rates among western industrial nations.

It is also important to recognize that most European nations out perform Canada on these basic indicators.

These indicators highlight the quandary which Canadian policy-makers face. The United States has chosen an approach to social policy which results in lower taxes and lower government expenditures but also results in lower health status and social stability than other western industrial nations. European countries, on the other hand, have tended to opt for higher tax burdens, higher levels of expenditure and higher degrees of health status and social stability.

Canada tends to be mid-way between these two extremes. If Canada is to maintain a greater commitment to social supports than the U.S., without the development of a massive public deficit, the question becomes - how do we increase the tax base while maintaining a competitive position with the U.S.?

Corporate Taxation

The need to maintain corporate taxation at lower levels, particularly for goods exported to the U.S., is typically justified on the basis of competitiveness. This issue, for example, was the primary justification for removing the manufacturers' sales tax in favour of the Goods and Services tax.

In comparing corporate tax rates, however, it is important to include employers social security contributions, which tend to be three to four percentage points lower in Canada. Insofar as corporate tax rates are applied only to profits while social security contributions are applied to the entire payroll of a company, this represents a significant cost advantage to Canadian companies. Accurate comparisons between the corporate tax systems in the two countries is also made difficult by the fact that the corporate/personal income tax systems are more fully integrated in Canada than in the U.S.

It is important to note that taxation is only one factor in the cost-of-production and, in turn, the price of Canadian produced goods in the American market are determined by more than just the cost-of-production. The other major variable affecting the price of Canadian goods in the American market is the value of the Canadian dollar, relative to U.S. currency. As the Canadian dollar falls in value against the U.S. dollar, the price of Canadian goods also falls.

Consumption Taxes

Personal consumption taxes affect the competitiveness of Canadian retailers. Given the proximity of a large portion of the Canadian population to U.S. border-communities, it is relatively easy for Canadians to shop in the U.S. The

importance of this factor has increased recently as a result of the Goods and Services Tax and the Free Trade Agreement.

Even before the GST was implemented, Canada relied upon consumption taxes to a much greater degree than the U.S. and this tended to increase the prices of goods in Canada, relative to the U.S.

Taxes on Personal Income and Wealth

There are also ongoing concerns about higher levels of taxes on personal income and wealth with respect to the development of a "brain drain" among talented high-income Canadians to the "tax-haven" of the U.S. This concern is often used to justify the need to keep Canadian tax rates below those of the European models and closer to those of the U.S.

One of the problems with this analysis is that it ignores the differences in private/public expenditures between the two countries. For example, one of the reasons that taxes are somewhat higher in Canada is because the public sector provides certain services which must be paid out of private incomes in the U.S. Health insurance is a commonly cited example of this difference, although educational expenditures are also relevant.

This argument also ignores the quality-of-life differences between the two countries and the fact that these quality-of-life differences can also have significant economic consequences. For example, a recent article in the Financial Post magazine which compared the two countries, suggested that executives living near large American cities are often forced to send their children to costly private schools because of the deteriorated state of many U.S. urban school systems.[16] The deterioration of this school system is, in turn, a result of the kind of under-funding which results from the lower tax burden in the U.S. This can, however, result in a higher private financial burden due to the costs of private school education to the individual.

It is also noteworthy that during the next twenty years, both Canada and the U.S. are going to have a "surplus" of potential senior managers because of the combined affects of the maturation of the post-war baby-boom and the increased degree of labour force participation by females.[17] This demographic factor calls into question, the extent to which American companies will be "raiding" Canadian enterprise to recruit senior managers. The likelihood of this occurring is further reduced by the growing trend in the U.S. to recruit more minority-member and female senior executives.

Conversely, the surplus among potential managers in the Canadian population would suggest that there will be more than ample capacity to replace any Canadian managers who do choose to move to the U.S. for reasons of taxation.

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16 Kohl, H. Has God Blessed America. Financial Post Moneywise, October 1988.

17 Food, D. and Venne, R. Population Pyramids and Promotion. Canadian Public Policy, December 1990, 387-398.

It is also notable that the fear of a "brain drain" has been raised within one profession - medicine - on at least two occasions. During the introduction of Medicare and, more recently, during the banning of extra-billing by physicians in the Province of Ontario. Following these two incidents, however, there has not been any evidence that the Canadian health care system has suffered from a drain of talented physicians to the U.S.

Based upon the above considerations, there appears to be justification for questioning the extent to which the fear of a "brain drain" due to personal taxation differentials is a relevant factor in the debate about tax policies.

It is also noteworthy, that the U.S. already taxes individual wealth and inheritances at a higher rate than they are currently taxed in Canada.[18]

Conclusion

Based upon the foregoing discussion, it is possible that our level of competitiveness with the U.S. would be least affected by an increase in personal income and wealth taxes, rather than increases in corporate or consumption taxes. This conclusion is based upon the following considerations -

1. We question the legitimacy of concerns related to a tax-induced "brain drain" to the U.S. for the following reasons -

    a) the changing demographics in the U.S. and Canada are producing a large surplus of middle and senior managers in both countries.

    b) the higher levels of personal expenditures for services in the U.S. which are provided through tax-funded government programs in Canada.

    c) the quality-of-life trade-off.

2. We also question concerns about the extent to which higher wealth and inheritance taxes in Canada would result in a movement of wealth to the U.S., given that the U.S. already taxes wealth and inheritance to a greater extent than it is taxed in Canada.

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[18] Social Planning and Research Council. Patterns of Taxation: International Comparisons. Taxation Review Task Force, Discussion Paper #1, 1988.

TABLE XI.1

Quality of Life Measures:
Canada and United States

	Canada	U.S.
Poverty Rates[1]		
All Persons	12.1	16.9
Under 24 yrs.	22.7	28.0
65 - 74 yrs.	11.2	17.8
75 + yrs.	12.1	25.5
Divorces/1,000[2]	2.4	4.8
Murder Rate[2]	2.2	8.6
Male Life Expectancy[2]	73	72
Female Life Expectancy[2]	80	79
Maternal Mortality Rate[2]	3	9
Infant Mortality Rate[2]	7	10
Growth in GDP (Annual Averages)[3]		
1973 - 1979	4.2	2.4
1979 - 1986	2.7	2.4
1960 - 1986	4.4	3.2
Growth in Real GDP Per Person Employed[3] (Annual Averages)		
1973 - 1979	1.3	0.0
1979 - 1986	1.0	.9
1960 - 1986	1.9	1.2

Sources:

1 Ross, D.P., Shillington, R., The Canadian Fact Book on Poverty. Canadian Council on Social Development, 1989.

2 The Economist, Book of Vital World Statistics. London: The Economist Books Ltd., 1990.

3 Historical Statistics 1960 - 1986. Paris: OECD, 1988.

XII. THE JAPANESE VARIANT

Japan represents a unique variant of North American and European approaches to social welfare. Its demographic structure is very similar to that of Canada but its level of public expenditures is significantly lower. With respect to both tax-burdens and public expenditures, Japan is similar to the U.S. but it has managed to maintain these low levels of expenditure without the social and health effects which appear to accompany the U.S. model.

The task force, therefore, examined the "Japanese approach" in order to arrive at some conclusions about the Japanese variation. Given the unique nature of corporate involvement in Japan, the analysis utilized, in addition to statistical data, qualitative material from a 1986 book by Akio Morita, the Chairman and CEO of Sony Corporation

Expenditures

The level of public expenditures in Japan are markedly lower than in Canada. In 1986, total outlays by government accounted for only 33.1% of the GDP in Japan while the corresponding figure for Canada was 46.2%.

Social security spending was only slightly lower in Japan (11.9% of GDP versus 12.3%) and a significantly lower level of public debt in Japan resulted in lower expenditures on interest payments.

Revenues

Tax revenues, as a percent of GDP, were also significantly lower in Japan than in Canada - 28.8% of GDP, compared to 37.5% in Canada.

Within the Japanese tax structure, a much higher proportion of these revenues came from corporate income tax and social security contributions and a markedly lower proportion were raised from personal income taxes and taxes on goods and services.

The level of dependence on property taxes were similar in both countries although Japan made more extensive use of estate taxes and taxation on financial and capital transactions.

The high rate of dependency on corporate taxation reflects the fact Japan has the highest overall corporate tax rate of any industrial country. According to a study by the American Congressional Research Service, additional municipal taxes mean that the total tax rate on manufacturing in Japan is 50.5%[19]. The comparable rate in the U.S. is only 27.7%. In addition, Japan allows for no accelerated depreciation and the Japanese tax system contains relatively few loopholes.

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19 Morita, A. Made in Japan, N. Y., E.P. Dutton, 1986.

With respect to personal income taxes, Japan has one of the most steeply progressive systems of taxation among industrial countries. As a result of a number of basic exemptions, the bottom third of the work force pay no income tax.

Unemployment Expenditures

Between 1980 and 1986, the annual growth rate of the Japanese GDP was 3.8% - higher than the corresponding Canadian rate of 2.7%. Among the major seven industrial countries, Japan ranked first in GDP growth while Canada ranked second.

Employment growth during that period, however, was markedly higher in Canada than in Japan. The average annual rate of employment growth for Canada was 2.9%, compared to only .7% in Japan. Despite the much more rapid rate of job creation in Canada, Japans unemployment rate was significantly lower - an average of 1.9% compared to 7.2%.

Part of the reason for this anomaly lies in the differential rates of labour force growth within the two countries - the Canadian labour force grew, on an annual basis, at twice the rate of the Japanese labour force - 2.0% per annum versus 1.0% per annum. This in turn, was due to dramatic differences with respect to trends in female labour force participation between the two countries.[20] As presented below, Japan had the highest rate of female labour participation among the largest OECD economies in 1965, while Canada had one of the lowest.

By 1987, however, the participation rate in Japan had actually decreased slightly, while the Canadian rate increased by 20.3 percentage points - to the highest rate among the seven nations.

Country	Female Labour Force Participation	
	1965	1987
Canada	34.8	55.1
U.S.	37.6	54.0
U.K.	39.7	48.6
France	37.9	44.5
West Germany	40.4	40.3
Italy	29.9	35.3
Japan	50.7	48.6

Given the lower rate of unemployment in Japan, expenditures on labour market programs and economic services in general were much lower in that country than in Canada. Labour market program expenditures accounted for .59% of GDP in Japan in 1986 and 2.24% in Canada.

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20 Chawla, H. Labour Force Participation: An International Comparison. Perspectives on Labour and Income, Winter 1990.

The other notable factor which has some effect on Japanese unemployment rates is the practice of "life-time employment" by some of Japan's larger corporations. The guaranteed job security which is implicit in this approach forces these industries to avoid lay-offs and, consequently, has the effect of maintaining relatively low levels of unemployment in the affected sectors.

Although considerable controversy does exist about the actual prevalence and practice of life-time employment policies in Japan, there does appear to be a distinct difference between the willingness of Japanese and North American businesses to lay off employees. Akio Morita, the chairman of Sony, addressed these differences in his 1986 book, Made in Japan, in a section of the publication which discussed the extensive use of "outsider" managers in American companies -

> "Recently one of these outsiders came into an American company; closed down several factories, laid off thousands of employees - and was hailed by other Executives in articles in the Wall Street Journal as a great manager. In Japan such a performance would be considered disgraceful. Closing factories and firing employees . . . in a business slump may be the expedient and convenient thing to do and may make the balance sheet look better at the end of the next quarter, but it destroys the company spirit. And when the business rebounds, where will the company go to get experienced workers who will produce quality goods and work hard and loyally for the company (pg. 200)."[21]

According to Morita, Japanese business is more willing than North American business to sacrifice short-term profits for long-term growth. This willingness may be due, in part, to differences in the financing of enterprise. In North America, the primary mode of financing is equity-financing through the stock market which, in turn, creates strong pressures to produce short-term returns in order to satisfy investors. In Japan, however, debt financing through bank-borrowing is used much more extensively. This means that Japanese companies tend to carry much higher debt loads the North American companies but it allows them to be less concerned about short-term returns.

According to a 1987 analysis by Kuttner, the U.S., the U.K., and Canada are unique in their approach to financing business investment -

> "In the United States, the United Kingdom, and Canada, commercial banks are far less involved in either the financing or the management of business firms, and companies rely largely on retained earning and equity issues to provide investment capital. But in much of continental Europe and in Japan, debt finance is the overwhelming source of investment capital for industry. During the 1970s for example, the ratio of debt to equity fluctuated between 50 and 60 percent in both the United States and the United Kingdom. In West Germany the ratio of debt to equity was almost 100 percent. In France it approached 150 percent, in Sweden it exceeded 175 percent and in booming Japan, the ratio rose from 229 percent in 1970 to over 350

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[21] Morita, A. Op cit

> percent by 1977 . . . Apparently debt financing also has its virtues. It can liberate management from the tyranny of the short-term balance sheet and lead to a more reasoned planning for long-term growth. Moreover, in the case of a rapidly growing firm, the greater debt financing increases the capacity of the firm to expand, notwithstanding the constraints of its own stream of retained earnings and the limited patience of its investors (pg 86-87)."[22]

It is worth noting, however, that debt-financing also has its disadvantages, particularly during times of high interest rates when pressures to meet monthly payments can also divert capital away from needed investment in plant, equipment and human resources. An extensive use of debt-financing requires a very close working relationship between banks and industry - a hallmark of both the Japanese and West German economies.

The primary issue appears to relate to the willingness of investors to take a long-term view to investment returns regardless of the instrument of investment. Investments in research and development, new ventures and other long-term sources of wealth, require a readiness to forego short-term returns for potentially greater long-term returns and the Japanese appear to be better able to tap these sources of investment.

In summary, then, relatively low rates of unemployment in Japan reduce the need for a significant investment of public funds in labour force programs. It is notable, however, that Japan's lower levels of unemployment, relative to Canada, were not due to superior rates of job creation. On the contrary, the Canadian economy out-performed the Japanese economy with respect to employment growth by a factor of almost three and a half.

It is probable that Japan's lower levels of unemployment were due to a variety of labour force and policy issues. The rate of labour force growth in Canada was twice that of Japan and this was largely due to a dramatic increase in female labour force participation in Canada. In addition, differential attitudes and expectations towards employee lay offs, business financing and returns on investment also play a probable role in a Japanese economy which maintains very low rates of unemployment.

Education Expenditures

In 1983, public expenditures on education in Japan amounted to 5.1% of GDP. This was lower than the corresponding figure of 7.0% in Canada.

This difference was not attributable to differences in the demographic structure of populations in the two countries. Persons aged 0 to 14 accounted for 21.5% of the population in both countries. Part of the difference may have been due to the higher concentration of students at the post-secondary level in Canada. According to a 1981 OECD study, 4853 of every 100,000 Canadian students

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22 Ibid

were enrolled in post-secondary institutions. The corresponding figure for Japan was only 1987.

In his 1987 book on Japanese Society, the Tokyo-based British businessman Peter Tasker had this to say about the Japanese educational system -

> "Despite the high regard in which education is held, the resources committed are not exceptional. Japan spends a lesser proportion of her GDP on education than is usual in the West, and teacher-pupil ratios are high. In state schools a teacher may be confronted with a class of seventy pupils, some of whom have to use binoculars to read the black board. Particularity within the metropolitan areas, the quality of facilities is poor."[23]

Health Expenditures

In 1986, public expenditures on health accounted for 4.0% of the GDP in Japan and 6.2% of the GDP in Canada. As in the case of education, the differences in expenditure level do not appear to be demographically based. In 1986 the two countries had almost equal proportions of the population aged 65 and over.

Both countries have government-sponsored universal health insurance, although the Japanese plan requires that users pay 10% of the cost.

Japan had fewer physicians per 100,000 population than Canada (15.1 and 19.6 respectively) and had a lower concentration of elderly persons living in institutions. In 1981, 17.5% of Canadians aged 75 and over were residing in institutions while the corresponding figure for Japan was only 5.8%.

In summary then, Japanese expenditures on health care as a percent of GDP were lower than Canadian expenditures, despite almost identical concentrations of persons aged 65 and over in both countries. The lower costs in Japan may have been due to a number of factors -

1. User fees of 10% within the health insurance plan;
2. Fewer physician per capita;
3. A lower concentration of elderly persons residing in institutions.

Pensions

According to UN figures, per capita expenditures for pensions in Japan in 1980 were $191 dollars (U.S.). The corresponding figure for Canada was $303 dollars (U.S.). Among western industrial countries, both Canada and Japan are at the low end of pension expenditures largely because of relatively low concentration of elderly persons in their populations.

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[23] Tasker, P. Op cit

It is noteworthy, however, that the Japanese population is aging at a much faster rate than any other industrial country. The Japanese have the longest life expectancies of any western country and by 2020, Japan will be second to only Sweden in terms of the concentration of persons 65 and over.

According to Tasker (1980) this trend will have dramatic effects on Japanese society -

> "Competitiveness is certain to suffer. Throughout her rise to prosperity, Japan has had the great advantage of the industrialized worlds most favourable balance of productive to non-productive population. As this alters, economic dynamism will diminish. Whether through public or private financing, the Japanese economy will have to devote less resources to capital investment and more to current expenditure. Increasing strains will be placed on the comparatively undeveloped social welfare systems (pg. 107)."[24]

Income Distribution

No discussion of the Japanese economic and social structure would be complete without reference to the issue of income distribution. As referenced in Chapter III of this report, Japan has the most equitable distribution of incomes among western industrial nations and, consequently, possesses one of the lowest incidences of poverty.

In addressing the issue of income distribution, it is important to recognize that a significant proportion of Canadian government expenditures are designed to address the implications of poverty, either directly or indirectly. This is obviously true of income maintenance payments and such programs as child tax credits. Given the strong relationship between poverty and such social problems as mental illness and drug abuse, it is also true that expenditures in those areas are also designed to respond to some of the more notable effects of poverty.

The relationship between income distribution and health expenditures, however, is less well-known. After a thorough review of the literature, the Premier's Council on Health Strategy for the Province of Ontario reached the following conclusion - "There is a strong relationship between socio-economic status and health status. The evidence indicates that when socio-economic differences are narrowed, population health status improves" (pg. 15). It is notable that this report made specific mention of Japan as an example of a nation with an equitable distribution of incomes and a very high level of population health status.

It is highly probable, therefore, that a significant proportion of government expenditures in Canada are a direct result of the need to mitigate the negative social effects of our inequitable distribution of incomes. In the case of Japan, these expenditures are not needed because the more equitable distribution of incomes reduces critical demand factors.

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[24] Ibid

Conclusions

At first glance, Japan appears to fit the profile of a free-market capitalist economy with low proportions of GDP devoted to social welfare and taxation. On the other hand, the strong partnership between business and government with respect to economic planning has earned Japan a reputation as one of the leading "planned" economies of the post-war period.

To confuse the issue even further, Japan has an income distribution which is almost 50% more equitable than the North American distribution of incomes and one of the most steeply progressive tax systems in the world. The egalitarian nature of the income distribution in Japan has reduced the need for large programs of income redistribution, through the tax system, to combat poverty.

In his 1986 book "Made in Japan", the chairman and CEO of Sony Corporation, Akio Morita, helped to explain some of the seemingly contradictory nature of the Japanese economic structure -

> "In Paris not too long ago someone said rather innocently to me that Japan is a capitalistic country. I said that it would appear so, but that actually it would be more accurate to say Japan has a socialistic and equalitarian free economic system. When the laws were changed after the war, it appeared to many Americans as well as Japanese that the swing to the left could be dangerous. The labour laws that made it virtually impossible to fire people seemed a terrible intrusion into the traditional discretionary powers of management, especially to the older managers. But they were forced to accept these laws and they turned them to everyone's advantage. Japanese managers thought that if every one could have a familial attitude . . . perhaps it would be easier to pull Japan out of the hole in which it found itself. That was the spirit that created what an American first called "Japan Inc." (pg. 180)."[25]

With respect to the very high level of corporate taxation in Japan, Morita had the following to say -

> "To put it bluntly, whether we like it or not, the government is a partner in our business without owning a single share of Sony stock or running any risk . . . The Japanese government takes away more than 50 percent of our profits and that in a sense makes it a majority partner. So from the governments viewpoint, it wants its partner to work hard and make a profit. By doing so, business is able to keep people employed, enabling the company and its employees to pay taxes rather than to go on the public dole. This is done with a long-range viewpoint (pg. 176)."[26]

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[25] Morita A. Op cit

[26] Morita A. Op cit

These quotes, then, help to explain the apparently contradictory nature of the Japanese economic and social structures. Stringent labour laws forced Japanese companies to adopt a "life-time employment" mode of operation which, in turn, forced the development of new management styles which have become an intrinsic cause of the Japanese success. At the same time, unusually high rates of corporate taxation have forced a business-government partnership which must be mutually supportive.

These factors, coupled with a system of financing which discourages a pre-occupation with short-term returns on investment in favour of longer term perspectives and a relatively egalitarian distribution of incomes, have created a socio-economic system in Japan which is unique in the world and which defies simplistic categorization.

Based upon all of these considerations it is probably accurate to conclude the Japan has managed to "escape" the need for large social expenditures because of significant structural factors which tend to prevent the development of problems which require social interventions -

1. Restrictive labour laws and an approach to human resource management which limits the demand for unemployment compensation. This, in turn, has been facilitated by rapid economic growth, coupled with a relatively slow growth in the labour force and a relatively young population which has diminished the need for pension expenditures.

2. A very egalitarian distribution of incomes which have reduced the need for income re-distribution programs to combat poverty.

JAPAN/CANADA COMPARISON

Expenditures	Japan	Canada
Total Outlays % GDP (1986)	33.1	46.2
Current Disbursements % GDP (1986)	27.4	43.0
Government Final Consumption % GDP (1986)	9.9	20.0
Social Security % GDP (1986)	11.4	12.3
Net Debt Interest % GDP (1986)	2.6	4.1
Subsidies to Business % GDP (1986)	1.1	2.0
Labour Market Programs % GDP (1986)	.59	2.24
Training	.03	.22
Income Maintenance	.42	1.68
Health % GDP (1986)	4.0	6.2
Education % GDP (1986)	5.1	7.0
Defence % GDP (1986)	.9	1.7
Net Lending % GDP (1986)	-2.1	-6.7
REVENUES		
Tax Revenues % GDP (1986)	28.8	37.5
% of Tax Revenues by Source (1986)		
Corporate Income Tax	20.7	8.1
Personal Income Tax	25.1	37.0
Employee Social Security	10.9	4.8
Employer Social Security	15.4	8.7
Property Taxes	10.9	9.4
Immovable	5.8	8.2
Wealth	n/a	0.7
Estate	1.4	.01
Financial/Capital	3.5	n/a
Goods and Services	13.4	29.7
Value-Added	n/a	.0
Sales	n/a	14.6
Excise	6.9	6.1
Other	6.5	9.0
INDICATORS		
% Population 0 to 14	21.5	21.5
Students/100,000 Third Level	1987.	4853.
Enrolment of 17 years old	90.	76.
% GDP (Education)/Each % 0 to 14	.24	.32
Unemployment Rate (1986)	2.8	9.5
Annual Employment Growth 79-86	.9	1.6

Annual Labour Force Growth 79-86	1.0	2.0
Annual GNP Growth 79-86	3.8	2.7
% Population 65 and over	10.3	10.4
Physicians/100,000	15.1	19.6
% Population 75+ in institutions	5.8	17.5

XIII. CONCLUSIONS

1) There is a general perception among Canadians that we are a highly-taxed nation. Relative to most other western industrial nations, however, our tax burden is relatively low. The perception of being "highly-taxed" may result, in part, from our proximity to the U.S., which is one of the least-taxed of western industrial nations.

2) There is also a general perception in Canada that we have a high rate of government expenditure on social security and labour market programs. Relative to other industrial nations, however, this is not true. Once again, this perception may arise from our close proximity to the U.S. which has one of the most limited systems of social support among western industrial nations.

3) Canada's higher level of commitment to social programs (relative to the U.S.) has resulted in an ongoing "high-wire act" whereby Canadian policy-makers have attempted to develop social supports, based upon more generous European models, while attempting to fund them through a level of taxation which is competitive with the U.S. The inevitable consequence of this policy has been a large public deficit, less generous programs than Europe and a higher taxation burden than the U.S.

4) In attempting to resolve this dilemma, Canadians have a few alternatives -

   a. To reduce expenditures and programs to the level of the U.S. and thereby bring expenditures in line with tax revenues.

   b. To increase tax levels to European levels.

   c. An integrated national policy which co-ordinates finance, education and investment to foster long-term economic growth and stability while, at the same time, ensuring a more equitable distribution of wealth. A more equitable distribution of personal wealth would maintain the degree of social stability and health status without a need for increased government expenditures.

5) Federal government policies during the 1980's have reflected the first of the above alternatives. In following this course, it is important to recognize that the U.S. is almost unique among western industrial nations with respect to its low level of commitment to social policy initiatives. It also possesses one of the highest levels of poverty and social instability and one of the lowest levels of health status among industrial nations.

6) The adoption of this course, therefore, implies a number of implications which need to be fully discussed and debated by the Canadian population. To adopt an American model is to live with its implications. Canada has managed to live "within the shadow of the U.S" while maintaining higher levels of social stability, health status and economic growth. Relative to many other western industrial nations, Canada has also maintained higher

levels of personal wealth and lower tax burdens. This personal wealth, however, is distributed more inequitably in Canada than in most other nations and, on this measure, we are very similar to the U.S. We have managed to mitigate the social and health effects of this inequity through a more comprehensive set of government programs than the U.S.

7) If deficit reduction is to become a national priority, the SPRC would favour an approach which represents a combination of taxation increases, a comprehensive national strategy to reduce the need for compensatory programs and clearly articulated spending priorities in health and social policy.

8) With respect to taxation increases, the SPRC supports the use of personal income/wealth and speculation taxes. These conclusions are based upon the following considerations:

   a) There is very little evidence from the actual performance of national economies that higher levels of taxation necessarily have negative implications for the economy.

   b) An emphasis upon personal income and wealth taxes will have the least effect upon our competitive position, relative to U.S. markets. We are concerned that increases in corporate and consumption taxes would have significant effect upon our competitive position.

   c) An emphasis upon personal income and wealth taxes could reduce the unusually large degree of inequity within the Canadian income distribution and thereby enhance social stability and health status without a need for greater expenditures in government direct service programs.

   d) An increased use of speculation taxes could provide incentives for investment in long-term wealth-generating strategies which are necessary to maintain national competitiveness.

9) The SPRC also recognizes the need for an integrated national strategy which co-ordinates finance, investment and education to resolve structural issues which require compensatory expenditures by government, particularly with respect to the direct costs of unemployment. We would argue that one of the most important structural issues relates to income distribution. To a considerable extent, the current rate of government expenditure in Canada is a result of the social and health effects of our inequitable distribution of incomes, relative to many other western industrial nations.

10) At the same time, we recognize that there are economic and political limits to the size of government expenditures. The experience of other nations who spend significantly more than Canada on public programs demonstrates that unmet needs continue to exist, despite the higher level of public expenditures. As a nation, we are hampered in responding to the expenditure issue by a lack of clear social, health and educational priorities to guide expenditure decisions. A comprehensive system of priorities is required to ensure that public resources are used for maximum impact.